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In The
Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

vs.

TEXTRON FINANCIAL CORPORATION,

Respondent.

On Petition For A Writ Of Certiorari To The Court Of Appeal Of California, Fourth Appellate District

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Did the California Court of Appeal commit constitutional error and improperly depart from this court's decision in *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996), by holding that a $1.7 million punitive damage award 20 times the relevant compensatory damages did not deny the defendant due process under the Fourteenth Amendment to the United States Constitution, where the case did not involve any of the special circumstances this court held might support a punitive damage award exceeding a single-digit multiple of compensatory damages?

2. Did the California Court of Appeal commit constitutional error and improperly depart from this court's decision in *BMW* by evaluating the amount of a punitive damage award in light of punitive damage awards in previous cases rather than in light of legislatively authorized civil and criminal penalties for comparable misconduct?

PARTIES TO THE PROCEEDINGS AND SUPREME COURT RULE 29.6 STATEMENT

Petitioner National Union Fire Insurance Company of Pittsburgh, Pennsylvania was the defendant, appellant, and cross-appellee below. Respondent Textron Financial Corporation was the plaintiff, appellee, and cross-appellant below. Petitioner is wholly owned by American International Group, Inc. and has one non-wholly owned subsidiary, JI Accident & Fire Insurance Co., Ltd. (Japan).

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PETITION FOR WRIT OF CERTIORARI

National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union) respectfully petitions for a writ of certiorari to review the judgment of the Court of Appeal of California, Fourth Appellate District, in this case.

OPINIONS BELOW

This court's October 9, 2001 order granting National Union's prior petition for a writ of certiorari is reported at 534 U.S. 947 (2001). The June 28, 2002 opinion of the Court of Appeal of the State of California, Fourth Appellate District, Division Three is unreported and reproduced in the appendix (App.) at 1. The January 29, 2001, opinion of the Court of Appeal is unreported and reproduced at App. 33. The May 29, 1996, judgment of the Superior Court of the State of California, Orange County, is unreported and reproduced at App. 62. The July 29, 1996, order of the Superior Court conditionally granting a new trial is unreported and reproduced at App. 72. The May 2, 2001 order of the Supreme Court of California denying National Union's petition for review from the Court of Appeal's January 29, 2001 opinion is unreported and reproduced at App. 78. The May 4, 2001 order of the Supreme Court of California correcting a clerical error in its May 2, 2001, order is unreported and reproduced at App. 79. The September 25, 2002 order of the Supreme Court of California denying National Union's petition for review from the Court of Appeal's June 28, 2002 opinion is unreported and reproduced at App. 80.

JURISDICTION

The judgment of the Court of Appeal was entered on June 28, 2002. App. 1. On September 25, 2002, the Supreme Court of California denied National Union's timely petition for review. App. 80. The jurisdiction of this court is invoked pursuant to 28 U.S.C.A. § 1257(a) (West 1993).

CONSTITUTIONAL PROVISION INVOLVED

The Fourteenth Amendment to the United States Constitution provides, in pertinent part: "No State shall . . . deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV, § 1.

STATEMENT OF THE CASE

A. Background.

This $1.7 million punitive damages case arises out of a claim for damage to a bus. In 1992, Il Sung Ko, the operator of a Los Angeles tour bus company, purchased an insurance policy covering his fleet of buses. Through Douglas Ferguson, an independent insurance broker, Ko obtained a National Union insurance policy issued by TRM International (TRM), an independent company acting as a "managing general agent" for National Union.[1]

[1] The term "managing general agent" is a term of art in the insurance field; it describes a company that markets and issues insurance policies on behalf of insurance companies pursuant to an agency agreement.

Respondent Textron Financial Corporation (Textron) had a security interest in one of Ko's buses and was named as loss payee on the National Union insurance policy. The policy's loss payable endorsement specified that if National Union were to cancel the policy, Ko and Textron would receive "the same advance notice."

After he purchased the National Union policy, Ko's financial situation declined, and he purportedly stopped using two of his buses, including the bus financed by Textron. Ferguson advanced Ko several thousand dollars in insurance premiums during that time. In late 1992, when Ko was unable to pay Ferguson back and after TRM, on behalf of National Union, threatened to cancel Ko's policy, Ko and Ferguson requested that TRM delete coverage of the two supposedly idle buses and issue a "premium credit" for the deleted vehicles. The deletion endorsement negotiated by the parties in late 1992 staved off cancellation of Ko's entire policy and enabled him to operate the rest of his fleet; in addition, Ferguson testified that the accompanying refund in the form of a premium credit would have repaid him for the substantial amount of money he had fronted to Ko. TRM prepared an endorsement to the policy stating that coverage for the bus had been deleted. Although TRM's records indicate that a copy of the endorsement was mailed to Textron, Textron denied receiving it.[2]

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[2] The deletion endorsement was effective as of December 1, 1992, but was not generated until February 1993. According to TRM, the delay was attributable to a backlog in administrative paperwork.

Ko continued to use the Textron-financed bus despite claiming to have garaged it, and in January 1993, the bus was involved in an accident. Ferguson notified the American International Adjustment Company (AIAC) – a company affiliated with National Union and vested with authority to investigate, approve, defend, or deny claims by or against National Union and its insureds – that the accident had occurred, and that Ko had previously requested the bus be deleted from the policy. A TRM supervisor confirmed Ferguson's statement and AIAC accordingly informed Ko that coverage would be denied.

Textron learned about the accident – and the deletion from the policy of the Textron-financed bus – several months later, after Ko defaulted on his loan obligations. Textron sued Ko for the balance due on the loan and secured a judgment against him, which Ko subsequently discharged in a bankruptcy proceeding. Textron also submitted a claim to National Union for $61,000 in property damage to the bus. After a lengthy investigation, National Union denied Textron's claim, concluding that it was not obligated under the policy to notify Textron of the cancellation by Ko.

B. Textron's lawsuit against National Union.

Textron sued National Union and AIAC, alleging breach of contract, breach of the covenant of good faith and fair dealing, conspiracy, and fraud.[3] Textron's contract

[3] Textron also brought claims against National Union and AIAC under California's unfair business practices statute. Those claims were

(Continued on following page)

claims were based on the parties' dispute over whether the loss payable endorsement required National Union to provide a lienholder with advance notice if a vehicle was deleted at the insured's request. Textron's conspiracy and fraud claims were grounded in a more sinister theory, however: that in fact the bus had not been deleted from the policy before the accident.

According to Textron, following the accident, Ferguson, Ko's broker, and various TRM employees had engaged in a complicated "post-accident underwriting" scheme to mislead both Textron and National Union into believing that coverage for the bus had been canceled before the accident, when in fact the bus was subject only to a "lay up credit" – a procedure sometimes used by a commercial insured with a fleet of vehicles who experiences a temporary lull in business. Under a lay up credit, coverage remains in effect, but the insurer provides a credit for the period of time the vehicle temporarily is out of service. Textron further claimed that TRM officials had fabricated various documents to support its position that the bus had been deleted from the policy. According to Textron, the purpose of this intrigue was to allow Ferguson, who had advanced Ko's premiums, to recoup those advances through a premium credit. Textron claimed that Ferguson and TRM were concerned that if National Union learned that the bus was still insured, it would refuse to provide a premium credit. Relying on a California statute, Cal. Civ. Code § 3294(b) (West 1997), which permits an award of punitive damages against a principal for the conduct of its

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dismissed prior to trial. In the same complaint, Textron also sued TRM and Ferguson for negligence. Both settled before trial.

"managing agent," Textron argued that punitive damages should be awarded against National Union because TRM was acting as National Union's managing agent.

At trial, the court ruled that National Union could not terminate Textron's rights as a loss payee without advance notice to Textron. Textron's contract damages claim, its claim for insurance bad faith, and its fraud and conspiracy claims were then tried to a jury, which found National Union liable for the money payable under the insurance policy. App. 63. The jury also concluded that National Union had committed insurance bad faith, rendering the company liable for approximately $86,000 in attorney's fees and costs incurred by Textron to prosecute this action. App. 64. The jury further concluded that AIAC had not made misrepresentations knowingly or with an intent to defraud, but that National Union had made such representations. App. 65-66. The jury awarded Textron $3,859.50 in compensatory damages on its fraud claim, representing the legal fees incurred when, relying on the purported misstatements that coverage had been deleted, Textron pursued Ko for damages. App. 67. The jury then awarded Textron $10 million in punitive damages against National Union. App. 70.

On National Union's motion, the Superior Court granted a conditional new trial, unless Textron agreed to a remittitur of the punitive damage award to $1.7 million. App. 72. Textron accepted the remittitur, App. 2, and National Union appealed.[4]

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[4] Textron filed a cross-appeal, claiming, among other things, that the trial court erred in granting the remittitur.

C. The first decision of the California Court of Appeal.

On appeal, National Union argued that even with the trial court's remittitur, $1.7 million in punitive damages was excessive and violated National Union's right to due process under the Fourteenth Amendment to the United States Constitution. National Union explained that the three "guideposts" set forth by this Court in *BMW of North America, Inc. v. Gore*, 517 U.S. 559, 574-575 (1996), mandated a finding that the trial court had erred in awarding Textron a colossal sum in punitive damages on a claim for a small fraction of that amount. Addressing each *BMW* factor at length, National Union argued that the trial court's punitive damage award constituted an "arbitrary deprivation of property" in violation of the Fourteenth Amendment's due process clause. *See Honda Motor Co. v. Oberg*, 512 U.S. 415, 430 (1994).

The Court of Appeal affirmed. App. 3. Citing its decision in *Stevens v. Owens-Corning Fiberglas Corp.*, 57 Cal. Rptr. 2d 525 (Ct. App. 1996), the court stated that "[o]n appeal, a judgment awarding punitive damages *is presumed to be correct* and will be reversed only if the record, *viewed most favorably to the judgment*, reflects the award is the result of passion or prejudice." App. 59-60 (emphasis added). The Court of Appeal concluded that the $1.7 million punitive damage award was "not excessive, nor does it violate National Union's constitutional right to due process of law." App. 61.

Following the Court of Appeal's decision, National Union filed a petition for review in the Supreme Court of California, arguing that the appellate court had failed to "conduct an independent review of the size of a punitive

damage award" to ensure the award conformed with the Fourteenth Amendment. Pet. for Review 1. The Supreme Court of California denied review without comment on May 2, 2001. App. 78.

D. National Union's first petition for writ of certiorari.

National Union filed a petition for writ of certiorari in this court, contending that the Court of Appeal failed to conduct a de novo review of the size of the punitive damage award as required by *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001). On October 9, 2001, this court granted the petition, vacated the Court of Appeal's January 29, 2001 opinion, and remanded the case to the Court of Appeal for reconsideration in light of *Cooper*. *National Union Fire Ins. Co. v. Textron Financial Corp.*, 534 U.S. 947 (2001).

E. The second decision of the California Court of Appeal.

On June 28, 2002, the Court of Appeal once again affirmed the judgment of the superior court. App. 1. Purporting to review the judgment de novo, it held the $1.7 million punitive damage award was not constitutionally excessive under the three *BMW* guideposts: (a) addressing the first *BMW* guidepost – "the degree of reprehensibility of the defendant's conduct" – the Court of Appeal held the conduct in question was sufficiently reprehensible to support $1.7 million in punitive damages even though TRM, not National Union, committed the wrongdoing, and National Union's liability for TRM's actions was merely vicarious, App. 28-29; (b) addressing

the second *BMW* guidepost – the "ratio to the actual harm inflicted on the plaintiff" – the Court of Appeal held that "[w]hile the compensatory award in this case was modest, in light of the reprehensible conduct attributable to National Union, the trial court properly imposed a punitive damage award sufficiently high to achieve the twin objectives of punishment and deterrence," App. 30; (c) addressing the third *BMW* guidepost – "the civil or criminal penalties that could be imposed for comparable misconduct" – the Court of Appeal held National Union was on notice it could be subject to a $1.7 million punitive damage award because "[i]t has long been common knowledge acts of bad faith by insurers could subject that party to significant punitive damage awards." App. 31. In addition, despite acknowledging that National Union's liability in this case was purely vicarious, based upon the conduct of its agent TRM, the Court of Appeal relied on a California statute which provides for a fine or imprisonment for *knowingly* assisting or conspiring with any person to conceal or fail to disclose the occurrence of an event that affects any person's right to insurance benefits. App. 31.

National Union again filed a petition for review in the Supreme Court of California. It argued (a) the Court of Appeal failed to satisfy its obligation under *Cooper*, 532 U.S. 424, to conduct a de novo review of the punitive damage award, and (b) when reviewed de novo in light of the three *BMW* guideposts, the $1.7 million punitive damage award violated National Union's federal due process rights. The Supreme Court of California denied review without comment on September 25, 2002. App. 80.

REASONS FOR GRANTING THE WRIT

I. INTRODUCTION.

In *BMW*, 517 U.S. at 574-575, this court identified three "guideposts" which courts should utilize in performing their constitutionally mandated duty to independently review a punitive damage award for excessiveness: (1) the degree of reprehensibility of the defendant's misconduct; (2) the disparity between the harm suffered by the plaintiff and the punitive damages award; and (3) the difference between the punitive damage award and the civil or criminal penalties authorized or imposed in comparable cases. *See also id.* at 583. This case offers an appropriate opportunity for the court to provide needed guidance regarding proper application of the second and third guideposts.

(a) Prior decisions of this court indicate that, except in limited circumstances, punitive damages should not exceed a modest single-digit multiple of compensatory damages. Nonetheless, in practice the second guidepost plays little, if any, role in the assessment of whether a punitive damage award is constitutionally excessive – numerous post-*BMW* decisions have upheld punitive damages that substantially exceed a single-digit multiple without regard to whether the circumstances which this court held will allow a larger multiple are present. Consequently, clarification from this court is necessary if that guidepost is to function as intended: to provide fair notice of the severity of the penalty likely to be imposed for prohibited conduct and meaningful guidance for appellate review of punitive damages.

This court has granted certiorari in *State Farm Mutual Automobile Insurance Co. v. Campbell*, 2001 Ut.

89, *cert. granted*, 70 U.S.L.W. 3741 (U.S. June 3, 2002) (No. 01-1289), to decide whether a $145 million punitive damage award that is 145 times compensatory damages violates federal due process. However, even if it reverses the Utah Supreme Court's judgment in *State Farm*, this court's decision may not provide guidance in the situation that more typically confronts lower courts on a regular basis and is presented by this case: a punitive damage award that, while nowhere near the monstrous award in *State Farm*, nonetheless substantially exceeds the single-digit multiple that prior decisions of this court have held is constitutionally permissible.

(b) As applied by the lower courts, the third *BMW* guidepost – the civil or criminal penalties authorized or imposed in comparable cases – similarly has failed to provide fair notice and a meaningful check on grossly excessive awards. Once again, this case is illustrative. In holding the $1.7 million punitive damage award was not constitutionally excessive when examined under that guidepost, the Court of Appeal stated: "It has long been common knowledge acts of bad faith by insurers could subject that party to significant punitive damage awards." App. 31. However, enormous punitive damages were precisely the problem that prompted this court to impose constitutional limitations on the size of those awards. Consequently, the Court of Appeal's reliance on those possibly unconstitutional pre-*BMW* awards to uphold the award here was circular and illogical and ignored this court's admonition to look to "legislative judgments concerning appropriate sanctions for the conduct at issue." *BMW*, 517 U.S. at 583. Unfortunately, the Court of Appeal's opinion is not an aberration; to the contrary, post-*BMW* decisions frequently hold a punitive damage award

is not excessive under the third guidepost so long as similar awards were made in prior cases.

To provide proper guidance regarding the second and third *BMW* guideposts, we urge this court to grant certiorari and consider this case in conjunction with *State Farm*. In the alternative, we request that the court defer a decision on this petition until it has decided *State Farm*, and then reverse or remand for reconsideration in light of its decision in that case. *See, e.g.*, *Keney v. New York*, 388 U.S. 440 (1967).

II. THIS COURT SHOULD CLARIFY THE CIRCUMSTANCES, IF ANY, IN WHICH PUNITIVE DAMAGES MAY EXCEED A SINGLE-DIGIT MULTIPLE OF COMPENSATORY DAMAGES.

In *BMW*, this court noted that "perhaps [the] most commonly cited indicium of an unreasonable or excessive punitive damages award is its ratio to the actual harm inflicted on the plaintiff." *BMW*, 517 U.S. at 580. This guidepost, like the other two delineated in that opinion, derives from the "fair notice" concept of due process. Due process requires "adequate notice of the magnitude of the sanction" that might be imposed for prohibited conduct. *Id.* at 574. As this court's decision in *BMW* establishes, subject to limited exceptions which are not present in this case, the ratio should not exceed a modest single-digit multiple of compensatory damages.

After noting that "the principle that exemplary damages must bear a 'reasonable relationship' to compensatory damages has a long pedigree," *BMW*, 517 U.S. at 580, this court cited to early English statutes which "provided for double, treble, or quadruple damages," *id.* at

581, and to present-day federal statutes which provide for ratios of 1 to 1 and 2 to 1. *Id.* 581 n.33. *See, e.g.*, 15 U.S.C.A. § 15 (West 1997) (treble damages – i.e., a 2 to 1 ratio – for antitrust violations); 15 U.S.C.A. § 1117(a) (West 1998) (treble damages for trademark infringement); 18 U.S.C.A. § 1964(c) (West 2000) (treble damages for RICO violations); 35 U.S.C.A. § 284 (West 2001) (up to treble damages for patent infringement). *See also Pac. Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1, 23-24 (1991) (ratio of 4 to 1 between punitive and compensatory damages was "close to the line . . . of constitutional impropriety.")[5]

Although this court "rejected the notion that the constitutional line . . . is marked by a single mathematical formula," *BMW*, 517 U.S. at 582, it nonetheless identified only a few circumstances as grounds for departure from a low multiple: (1) cases involving "low awards of compensatory damages," i.e., where "a particularly egregious act has resulted in only a small amount of economic damages"; (2) where "the injury is hard to detect"; and (3) where "the monetary value of noneconomic harm might have been

[5] Plaintiffs seeking to uphold significant ratios between punitive and compensatory damages frequently assert that in *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443 (1993), this court upheld a $10 million punitive damage award where compensatory damages were only $19,000, a ratio of over 526 to 1. In fact, this court looked to the ratio between the punitive award and the actual and potential harm to the plaintiff in that case. 509 U.S. at 462. The plaintiff in *TXO* contended that the potential harm was between $5 million and $8.3 million, i.e., a ratio of between 1.2 to 1 and 2 to 1. *See* 509 U.S. at 461. Although the plurality apparently agreed that the plaintiff's estimation of potential harm was exaggerated, it nonetheless concluded that "the jury could well have believed that TXO was seeking a multimillion dollar reduction in its potential royalty obligation." *Ibid.* Thus, the ratio probably was not more than 5 to 1.

difficult to determine," prompting concern that the plaintiff might not be made whole. *Ibid.*

Nonetheless, the second *BMW* guidepost has been applied in a haphazard and wholly unpredictable fashion. While some courts have treated that guidepost as a meaningful restraint of the size of punitive damages, *see, e.g., In re Exxon Valdez*, 270 F.3d 1215, 1243-44 (9th Cir. 2001) (suggesting that ratio of between 12 to 1 and 17 to 1 constitutionally excessive because it greatly exceeded the 4 to 1 ratio that *Haslip* held was "'close to the line'"), many other courts have upheld awards substantially exceeding a single-digit multiple regardless of whether any circumstance which this court held would support a larger multiple is present.[6] Consequently, in practice the second guidepost fails to provide either fair notice of the severity of punishment for prohibited conduct or a meaningful check on excessive punitive damages.

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[6] *See, e.g., Paracelsus Health Care Corp. v. Willard*, 754 So. 2d 437, 445 (Miss. 1999), *cert. denied*, 530 U.S. 1215 (2000) (upholding ratios of 150 to 1 and 43 to 1 even though court acknowledged that none of the circumstances for large multiple delineated in *BMW* was present); *Weeks v. Baker & McKenzie*, 74 Cal. Rptr. 2d 510, 534 (Ct. App. 1998) (70 to 1 ratio); *Parrott v. Carr Chevrolet, Inc.*, 965 P.2d 440, 443 (Or. Ct. App. 1998) (26 to 1 ratio); *Harris v. Soley*, 756 A.2d 499, 509 (Me. 2000) (16 to 1 ratio); *Rhyne v. K-Mart Corp.*, 562 S.E.2d 82, 94 (N.C. Ct. App. 2002) (30 to 1 and 23 to 1 ratios); *Wilson v. IBP, Inc.*, 558 N.W.2d 132, 147-48 (Iowa 1996) (500 to 1 ratio); *Life Ins. Co. of Ga. v. Johnson*, 701 So. 2d 524, 534 (Ala. 1997) (12 to 1 ratio); *Romo v. Ford Motor Co.*, 122 Cal. Rptr. 2d 139 (Ct. App. 2002) (58.8 to 1 ratio); *Walston v. Monumental Life Ins. Co.*, 923 P.2d 456, 468 (Idaho 1996) (26.67 to 1 ratio); *Johansen v. Combustion Engineering, Inc.*, 170 F.3d 1320, 1339 (11th Cir. 1999), *cert. denied*, 528 U.S. 931 (100 to 1 ratio).

This case is typical. The ratio between the $89,000 award on Textron's tort cause of action – the only cause of action that would support punitive damages[7] – is 20 to 1. *See Zimmerman v. Direct Fed. Credit Union*, 262 F.3d 70, 82 n.9 (1st Cir. 2001) ("We believe that it is appropriate to construct the ratio by looking only to the count on which punitive damages were awarded."). Indeed, even if the relevant ratio is the 10 to 1 ratio between the punitive award and the combined $165,000 tort and contract award, it still substantially exceeds the 4 to 1 ratio which this court held was "close to the line . . . of constitutional impropriety." *Haslip*, 499 U.S. at 23-24.

However, this case involves none of the circumstances which this court identified as grounds for departure from a low multiple. *See BMW*, 517 U.S. at 582: (a) The compensatory damages – whether $89,000 or $165,000 – are not small, and the act in question – the failure to pay a $61,000 property damage claim by a major finance company – was not "particularly egregious"; (b) the injury – Textron's loss of its security interest in the bus and the attorney fees it incurred to recover policy benefits – are not hard to detect; and (c) because it is a corporation, Textron is incapable of suffering noneconomic harm. Moreover, "there [was] no suggestion that [Textron] was threatened with any additional potential harm" from the conduct in this case. *BMW*, 517 U.S. at 582.

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[7] Under California law, a punitive damage award may be based only on an award of tort damages, not contract damages. *Myers Bldg. Ind., Ltd. v. Interface Tech.*, 17 Cal. Rptr. 2d 242, 248 (Ct. App. 1993).

In sum, as applied in this and similar cases, the second *BMW* guidepost fails to provide fair notice regarding the severity of the punishment likely to be imposed for prohibited conduct and meaningful guidance for appellate review of punitive damage awards. We urge the court to grant certiorari in order to provide comprehensive guidance regarding the proper application of that guidepost.

III. THE COURT OF APPEAL'S RELIANCE ON PRIOR PUNITIVE DAMAGE AWARDS TO HOLD THE $1.7 MILLION AWARD WAS NOT EXCESSIVE WHEN COMPARED TO THE CIVIL OR CRIMINAL PENALTIES THAT COULD BE IMPOSED FOR COMPARABLE MISCONDUCT RENDERS THE THIRD *BMW* GUIDEPOST MEANINGLESS.

The third *BMW* guidepost is a comparison between "the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct. . . . " *BMW*, 517 U.S. at 583. This court explained that "a reviewing court engaged in determining whether an award of punitive damages is excessive should 'accord "substantial deference" to legislative judgments concerning appropriate sanctions for the conduct at issue.'" *Ibid.* It noted that the $2 million punitive damage award imposed on *BMW* in that case was "substantially greater than the statutory fines available in Alabama and elsewhere for similar malfeasance" and *BMW* therefore did not receive "fair notice that the . . . violation . . . [of the applicable statute] might subject an offender to a multimillion dollar penalty." *Id.* at 583-84.

As National Union explained in the Court of Appeal, the $1.7 million punitive award here is excessive under

the third guidepost because the maximum statutory penalty established by the California Legislature for the conduct in issue – insurance bad faith – is $10,000. Cal. Ins. Code § 790.035 (West 1993). That statute certainly did not provide National Union with fair notice that its denial of Textron's property damage claim would subject it to a seven-figure penalty.

Nonetheless, the Court of Appeal held National Union had "'fair notice'" it could be subjected to a $1.7 million punishment, and that the award therefore was not excessive under the third *BMW* guidepost, because "[i]t has long been common knowledge acts of bad faith by insurers could subject that party to significant punitive damage awards." App. 31.

However, this court's decisions admonishing that the due process clause prohibits '"grossly excessive"' punishments on a tortfeasor, *see BMW*, 517 U.S. at 562, were a direct response to the fact that enormous punitive damage awards were being rendered and affirmed with increasing frequency. *See, e.g.*, *Haslip*, 499 U.S. at 18 ("We note once again our concern about punitive damages that 'run wild.'"). Consequently, in holding that a person is entitled to "fair notice . . . of the severity of the penalty that a state may impose," *BMW*, 517 U.S. at 574, this court directed lower courts to look to "legislative judgments concerning appropriate sanctions for the conduct at issue," *BMW*, 517 U.S. at 583, *not* the punitive damage awards imposed by juries in prior cases. Since the "significant punitive damage awards" referred to by the Court of Appeal were precisely the problem this court was seeking to rectify when it delineated its three guideposts, the Court of Appeal's reliance on those awards to justify the punitive

damage award here was circular and illogical and effectively rendered the third guidepost meaningless.

Once again, this case is not an aberration. To the contrary, in addressing the third *BMW* guidepost, the lower courts frequently point to prior punitive damage awards in the jurisdiction to conclude the defendant had "fair notice" its conduct could result in a substantial award. *See, e.g.*, *Romo*, 122 Cal. Rptr. 2d at 166 ("[d]efendant has been on notice 'for more than a century' that California regards it as necessary to impose penalties related to the wealth of the defendant in order to achieve the goals of punishment and deterrence . . . [a]nd defendant has been on notice since at least 1971 that a week's profits amounting to about 1 percent of net wealth are not excessive punitive damages" (citation omitted)); *Cont. Trend Res., Inc. v. OXY USA, Inc.*, 101 F.3d 634, 641 (10th Cir. 1996), *cert. denied*, 520 U.S. 1241 ("[p]laintiffs point to cases from other states involving very large punitive damage awards. . . . Those cases, together with cases involving large awards in Oklahoma, . . . , provided sufficient notice to OXY of the potential for large punitive awards" (citations omitted)); *Williams v. Philip Morris Inc.*, 48 P.3d 824, 842 (Ct. App. 2002) *adhered to on reconsideration by* 51 P.3d 670 (Or. Ct. App. 2002) ("[t]o the extent that the issue involves adequate notice to defendant, the established Oregon law of punitive damages . . . was sufficient to alert defendant to the possible punishment for its fraudulent scheme" (citation omitted)); *Zimmerman*, 262 F.3d at 83 ("[s]ince the Legislature provided explicit notice that the violator of one of the provisions of Chapter 151B could be liable for punitive damages several times greater than the compensatory award in the same case, the appellants were sufficiently on notice that

retaliating against the plaintiff in violation of the statute potentially could subject them to a similar level of punitive damages"); *Simon v. San Paolo U.S. Holding Co., Inc.*, No. B121917, 2001 WL 1380836 at *12 (Ct. App. 2001) ("substantial punitive damage awards have been a reality in fraud cases for many years. . . . Our consideration of the third *BMW* factor leads us to conclude that San Paolo had fair notice that intentional affirmative acts of fraud may lead to a sizeable punitive damage award" (citation omitted)); *Walston*, 923 P.2d at 468 ("In Idaho punitive damages have long been allowed, and the special relationship between an insurer and an insured has been well defined. The state has set standards of practice in the insurance industry. There is no doubt that Monumental knew, if it paid attention, that severe penalties could follow from fraud in marketing and bad faith denial of benefits practice.").

In the view of these courts, one excessive punitive damage award justifies another, and no reference to legislative determinations of appropriate penalties is needed.

In sum, as applied in this and similar cases, the third *BMW* guidepost, like the second, fails to afford the fair notice required by due process and is essentially meaningless as a check on grossly excessive punitive damages. Certiorari should be granted to clarify that when examining a punitive award under that guidepost, a court should compare the award with the legislative penalties that

realistically might be imposed in comparative cases, not the punitive damages awarded in prior cases.[8]

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[8] The Court of Appeal also suggested the $1.7 million punitive damage award was not excessive under the third *BMW* guidepost because a California statute, Cal. Penal Code § 550(a)(10)(b) (West 1999), makes it a felony subject to fine or imprisonment to "knowingly assist or conspire with any person" to conceal or fail to disclose the occurrence of an event that affects any person's right to insurance benefits. App. 31. However, because the Court of Appeal acknowledged that National Union's liability was vicarious, based on its agent's wrongdoing, and that National Union's own fault was limited to its "self-imposed ignorance" of its agent's conduct, App. 29, it is wholly unreasonable to assume that any National Union officer could have been imprisoned under a statute which punishes "knowing" participation in the prohibited conduct.

CONCLUSION

The petition for writ of certiorari should be granted. In the alternative, the petition should be granted, the judgment of the Court of Appeal vacated, and the case remanded for further consideration in light of this court's decision in *State Farm*, No. 01-1289.

Respectfully submitted,

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IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORPORATION, Plaintiff and Appellant, v. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al., Defendants and Appellants.	G020323 (Super Ct. No. 734096) OPINION (Filed Jun. 28, 2002)

Appeals from a judgment and postjudgment orders of the Superior Court of Orange County, Nancy Wieben Stock and Raymond J. Ikola, Judges. Judgment and postjudgment orders affirmed.

Albert, Weiland & Golden, Marcus M. Kaufman; Stephan, Oringher, Richman & Theodora and Robert M. Dato for Plaintiff and Appellant.

Horvitz & Levy, Michell C. Tilner, Peter Abrahams; Lewis D'Amato, Brisbois & Bisgaard, R. Gaylord Smith and Michael W. Connally for Defendants and Appellants.

* * *

Plaintiff Textron Financial Corporation sued defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union) and others over its refusal to honor a claim for insurance benefits concerning property damage to a commercial bus in which plaintiff held a security interest. Plaintiff settled with two parties and proceeded to trial against National Union and American International Adjustment Company, Inc. (AIAC), National Union's claims adjuster. After a trial divided into three phases, the trial court entered judgment on a jury's special verdict awarding plaintiff $165,414.40 in compensatory damages and $10 million in punitive damages against National Union. The court entered judgment, including costs, for AIAC against plaintiff.

Both plaintiff and National Union filed postjudgment motions. The trial court denied National Union's motion for judgment notwithstanding the verdict and plaintiff's motion for a new trial, but conditionally granted National Union a new trial unless plaintiff agreed to reduce the punitive damage award to $1.7 million. Plaintiff agreed to the remittitur. The court also struck plaintiff's request for expert witness fees.

Both plaintiff and National Union appealed from the judgment and postjudgment orders. Plaintiff challenged the trial court's striking of its cause of action for unfair business practices, the judgment in favor of AIAC, including costs, the remittitur of punitive damages, and the denial of its request for expert witness fees. National Union attacked the punitive damage award on several grounds, and the trial court's refusal to offset the amounts plaintiff received in the pre-trial settlements.

In an unpublished opinion filed January 29, 2001, we affirmed the judgment and postjudgment orders in their entirety. National Union filed a petition for writ of certiorari with the United States Supreme Court. On October 9, the Supreme Court issued an order granting the writ, vacated our judgment and remanded the matter to us for further consideration in light of *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.* (2001) 532 U.S. 424. We granted the parties the opportunity to file supplemental briefs on the issue of whether the punitive damage award violates federal due process when reviewed under a de novo standard of review.

Having reviewed the matter in accordance with the United States Supreme Court's direction, we again affirm the trial court's judgment and postjudgment orders in their entirety.

FACTS

Il Sung Ko operated a tour bus company, Taeguk Tour and Sightseeing (Taeguk). Plaintiff loaned Ko funds to purchase a bus, receiving in return a security interest in the vehicle. The security agreement required Ko to insure the bus. Ko obtained a National Union liability insurance policy through D.W. Ferguson & Associates, Inc. (Ferguson), an independent insurance brokerage. The policy was issued through TRM International, Inc. (TRM), a company appointed by National Union to solicit, bind, write, and administer policies for its commercial bus program. The policy listed plaintiff as a loss payee and required National Union to mail plaintiff notice in advance if it cancelled the policy.

Taeguk suffered a downturn in business and Ko failed to timely pay his insurance premiums. In October 1992, TRM sent Ko notice it intended to cancel the policy. TRM did not send a copy of the cancellation notice to plaintiff. The policy terminated November 27.

Beginning in late October and throughout November, Ferguson and Taeguk discussed reducing the insurance premiums by deleting coverage for some of Ko's vehicles. Ferguson also corresponded with a TRM underwriter about the situation, proposing the issuance of a new policy covering only some of Ko's busses. The underwriter suggested an alternative whereby TRM would reinstate the original policy and give Ko a credit against his policy's premium if he agreed to certain conditions, which included delivering the license plates of two buses to Ferguson and temporarily suspending use of those vehicles. Plaintiff presented expert testimony that, unlike a transaction where a vehicle is deleted from a policy, the alternative approach implemented a procedure described as lay-up credit. Under a lay-up credit, the insured maintains coverage on a vehicle while it is not being operated.

Ko agreed to this proposal, and on December 1, TRM retroactively reinstated the policy effective November 27. The bus encumbered by plaintiff's security interest was one of the vehicles Ko intended not to use. Plaintiff did not receive notice of the policy reinstatement with the endorsement which reflected Ko's business received a premium credit due to the vehicle's non-use. National Union claimed it sent a copy of this endorsement to plaintiff, but plaintiff denied receiving it.

In January 1993, the bus encumbered by plaintiff's lien suffered extensive damage when it collided with

another vehicle on a public highway. At Taeguk's request, Ferguson submitted a notice of claim to AIAC. On February 4, TRM sent AIAC a notice verifying coverage for the vehicle and confirming plaintiff as a loss payee. However, after further correspondence with Taeguk and TRM, AIAC denied the claim, asserting the bus had been deleted from the policy before the accident. TRM prepared an endorsement deleting the bus from the policy (Number 8) on February 16. This endorsement purported to be effective as of December 1, 1992.

In late 1993, Ko defaulted on plaintiff's loan. Plaintiff then learned about the accident and contacted Ferguson concerning insurance benefits to repair the vehicle. Ferguson informed plaintiff the bus had been removed from the policy before the accident. Plaintiff sued Ko, recovering a judgment against him and incurring $3,859.50 in legal fees in the process. However, Ko filed bankruptcy and discharged the debt.

Plaintiff submitted a claim to National Union for benefits under the insurance policy. At that time, it possessed only a certificate of insurance, not a copy of the policy.

AIAC also handled plaintiff's claim. TRM informed AIAC the encumbered bus had been deleted from the policy before the accident and sent it a copy of endorsement Number 8. A certificate of mailing on that copy covered the part of the endorsement reflecting the date TRM had prepared it. After an AIAC claims manager discussed the matter with John Lavin, a senior underwriter with the division handling National Union's bus program, and Tom Spangenberg, TRM's president, AIAC advised plaintiff the claim was being denied. The basis of

the denial was that Ko deleted the bus from the policy before the accident, and TRM and AIAC concluded National Union's policy did not obligate it to give plaintiff advance notice of the deletion. National Union did not send plaintiff a copy of the policy until August 1994. Again, the mailing certificate covered the portion of endorsement Number 8 displaying the date on which it had been prepared.

PROCEDURAL BACKGROUND

The trial's first phase dealt with plaintiff's breach of contract claim against National Union. The court found, as a matter of law, the insurance contract's loss-payable clause constituted a separate agreement between plaintiff and National Union, obligating National Union to provide 30 days' notice of the policy's cancellation or the bus's deletion from it, and that National Union failed to comply with this requirement. The jury subsequently awarded plaintiff $61,513.80 under the policy.

The second phase involved plaintiff's causes of action for bad faith against National Union and fraud against both National Union and AIAC. The jury returned a special verdict finding National Union violated the policy's implied covenant of good faith and fair dealing and that it acted with oppression, malice, and fraud in doing so. The jury also returned a special verdict finding National Union liable for intentional misrepresentation and concealment and awarded plaintiff $3,859.80 in damages. Based on its interpretation of the jury's answers in the special verdict, the trial court entered judgment for AIAC on the fraud count.

During this phase, the trial court also ruled plaintiff could recover $30,268.16 in attorney fees as damages under *Brandt v. Superior Court* (1985) 37 Cal.3d 813. The parties stipulated plaintiff was entitled to $55,616.34 in costs pursuant to *Brandt*. Subsequently, the court denied National Union's request to offset the pretrial settlements plaintiff received from Ferguson ($26,500) and TRM ($62,500) against the compensatory award imposed on it.

The trial's third phase dealt with punitive damages. The jury awarded $10 million in punitive damages against National Union which the trial court subsequently reduced to $1.7 million. In addition, the judgment awarded plaintiff compensatory damages, consisting of the policy benefits plus interest, the legal expenses recoverable under *Brandt v. Superior Court, supra,* 37 Cal.3d 813, and the damages for fraud. Finally, the court awarded AIAC $10,277.52 in costs against plaintiff.

DISCUSSION

PLAINTIFF'S APPEAL

Demurrer to the Unfair Business Practices Cause of Action

The complaint's fourth count sought injunctive and restitutionary relief under Business and Professions Code section 17200 et seq. against National Union and AIAC for "engag[ing] in unfair competition" in the "handling [of plaintiff's] claim, and the claims of other persons." Plaintiff alleged National Union, "aided and abetted" by AIAC, "used misleading documents to falsely suggest that it would provide insurance . . . where it had no intention to do so," "falsely suggested that it would . . . provid[e] timely notice of [policy] cancellations," "misrepresented the terms and meaning of its policies . . . to provide a pretext for its

refusal to provide timely notice," and "engaged in a pattern and practice of wrongful and false cancellations of insurance policies. . . . "

Relying on *Moradi-Shalal v. Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, National Union and AIAC generally demurred to this count. The trial court sustained the demurrers without leave to amend. Citing *State Farm Fire & Casualty Co. v. Superior Court* (1996) 45 Cal.App.4th 1093, plaintiff contends the trial court's ruling was erroneous.

Moradi-Shalal held the Unfair Insurance Practices Act (Ins. Code, § 790 et seq.; UIPA) does not create a private cause of action against insurers who violate its provisions. (*Moradi-Shalal v. Fireman's Fund Ins. Companies, supra,* 46 Cal.3d at pp. 304-305.) This rule applies to both first party and third party claims. (*Maler v. Superior Court* (1990) 220 Cal.App.3d 1592, 1597-1598; *Zephyr Park v. Superior Court* (1989) 213 Cal.App.3d 833, 836-838.) While insurance companies are subject to California laws generally applicable to other businesses, including laws governing unfair business practices (Ins. Code, § 1861.03, subd. (a)), parties cannot plead around *Moradi-Shalal's* holding by merely relabeling their cause of action as one for unfair competition. (*Manufacturers Life Ins. Co. v. Superior Court* (1995) 10 Cal.4th 257, 283-284; *Maler v. Superior Court, supra,* 220 Cal.App.3d at p. 1598; *Safeco Ins. Co. v. Superior Court* (1990) 216 Cal.App.3d 1491, 1494.)

The specific allegations of wrongful conduct contained in plaintiff's fourth cause of action, using misleading documents and misrepresenting both the terms of the insurance policies and its obligations under them for its

own benefit, are the type of activities covered by the UIPA. (Ins. Code, § 790.03, subds. (a) & (h) .) In *Safeco Ins. Co. v. Superior Court, supra,* 216 Cal.App.3d 1491, the court ordered dismissal of an action which included a request for injunctive relief under Business and Professions Code section 17200 et seq. based on an insurer's allegedly unfair claims settlement practices. (*Id.* at pp. 1493-1494.) "Though the issue is one of first impression, we have no difficulty in deciding the Business and Professions Code provides no toehold for scaling the barrier of *Moradi-Shalal*. . . . To permit plaintiff to maintain this action would render *Moradi-Shalal* meaningless." (*Id.* at p. 1494.) Under the foregoing cases, merely alleging these purported acts constitute unfair business practices under the unfair competition law is insufficient to overcome *Moradi-Shalal.*

In a few cases, the Supreme Court has allowed an action against an insurance company under the unfair competition law where the alleged conduct constituted an unlawful restraint on trade under the Cartwright Act (Bus. & Prof. Code, § 16700 et seq.), even though it also violated the UIPA. (*Quelimane Co. v. Stewart Title Guarantee Co.* (1998) 19 Cal.4th 26, 43-44; *Manufacturers Life Ins. Co. v. Superior Court, supra,* 10 Cal.4th at pp. 283-284.) "This conclusion does not compromise the rule of *Moradi-Shalal* in any way. The court concluded there that the Legislature did not intend to create new causes of action when it described unlawful insurance business practices in section 790.03, and therefore that section did not create a private cause of action under the UIPA. The court did not hold that by identifying practices that are unlawful in the insurance industry, practices that violate the Cartwright Act, the Legislature intended to bar

Cartwright Act causes of action based on those practices." (*Manufacturers Life Ins. Co. v. Superior Court, supra,* 10 Cal.4th at p. 284.)

The case on which plaintiff relies, *State Farm Fire & Casualty Co. v. Superior Court, supra,* 45 Cal.App.4th 1093, held the plaintiff-insureds had sufficiently alleged a cause of action against their insurer under the unfair competition law based on allegations of conduct constituting common law fraud and breach of the implied covenant of good faith and fair dealing, even though the same conduct violated the UIPA. "While *Moradi-Shalal* clearly held that the Legislature did not intend to create new causes of action when it enacted section 790.03, it is also clear that the Legislature did not intend in any way to circumscribe the previously existing common law right of an insured to seek redress for an insurer's fraudulent deception or breach of the covenant of good faith implied in the policy. . . . Thus, . . . common law claims remain as a firm legal basis on which an insured may rely to seek redress against an insurer." (*Id.* at pp. 1107-1108.)

The persuasiveness of *State Farm* has been undercut by the Supreme Court's subsequent disapproval of its definition of "unfair" business practices. Quoting from *People v. Casa Blanca Convalescent Homes, Inc.* (1984) 159 Cal.App.3d 509, *State Farm* declared: "The test of whether a business practice is unfair 'involves an examination of [that practice's] impact on its alleged victim, balanced against the reasons, justifications and motives of the alleged wrongdoer. In brief, the court must weigh the utility of the defendant's conduct against the gravity of the harm to the alleged victim. . . . [Citations.]'. . . . [A]n 'unfair' business practice occurs when that practice 'offends an established public policy or when the practice is

immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers.' [Citation.]" (*State Farm Fire & Casualty Co. v. Superior Court, supra,* 45 Cal.App.4th at pp. 1103-1104, fn. omitted.)

In *Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.* (1999) 20 Cal.4th 163, the Supreme Court found this definition is "too amorphous and provid[es] too little guidance to courts and businesses." (*Id.* at pp. 184-185.) While *Cel-Tech Communications* limited its discussion to the context of an action between competitors, the court concluded, "any finding of unfairness to competitors under section 17200 be tethered to some legislatively declared policy or proof of some actual or threatened impact on competition," and that under Business and Professions Code section 17200, "the word 'unfair' . . . means conduct that threatens an incipient violation of an antitrust law, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law. . . . " (*Id.* at pp. 186-187, fn. omitted; see also *Schnall v. Hertz Corp.* (2000) 78 Cal.App.4th 1144, 1165-1167 [applying *Cel-Tech Communications, Inc.'s* standard in vehicle lessee's action against rental agency for allegedly concealing or obscuring the rental agreement's fuel service charge].)

Harmonizing *Moradi-Shalal's* holding with the foregoing decisions supports a conclusion the trial court properly sustained the demurrers to plaintiff's unfair competition claim. First, the holding in *Safeco Ins. Co. v. Superior Court, supra,* 216 Cal.App.3d 1491 supports this result. Second, this case is distinguishable from *Quelimane* and *Manufacturers Life* in two respects. Neither decision involved an action by an insured or a third party based on the insurer's alleged failure to comply with a policy or to

provide benefits. In *Quelimane,* parties who acquired real estate at tax sales sued title insurance companies for refusing to issue policies on their property. *Manufacturers Life* concerned an insurance agency's action against insurance companies for boycotting the agency. Also, in both cases the plaintiff alleged a Cartwright Act violation as the basis for its unfair competition cause of action. Finally, given the Supreme Court's disapproval of *State Farm's* "amorphous" definition of "unfair" practices and its focus on legislatively declared public policy, reliance on general common law principles to support a cause of action for unfair competition is unavailing.

Under these circumstances, the trial court properly found plaintiff failed to state a cause of action against National Union and AIAC for unfair business practices.

The Jury's Phase Two Findings

During the second phase, the jury returned a special verdict containing findings on the elements of two theories of deceit, intentional misrepresentation and concealment of a material fact. The jury's responses reflect it found both National Union and AIAC made representations of a material fact on which plaintiff justifiably relied to its injury and that both defendants made the representations "recklessly without knowing whether [they were] true or false." However, the jury concluded AIAC did not know the representations were false and did not make them with the intent to defraud plaintiff. On the concealment theory, the jury found both defendants concealed or suppressed a material fact which resulted in injury to plaintiff, but also found AIAC did not intentionally conceal or suppress a material fact with the intent to defraud plaintiff. In

addition, the jury concluded both defendants were "guilty of fraud, malice, or oppression in the conduct upon which [it] based [its] finding of liability. . . . "

When the jury returned its special verdict, the court discussed the inconsistency in the findings with counsel and ultimately ruled AIAC "is not liable for fraud or concealment." Plaintiff argues the trial court erred by construing the jury's findings to exonerate AIAC.

The distinction between a general and special verdict is that under the former a jury "pronounce[s] generally upon all or any of the issues," while the latter is one "by which the jury find the facts only, leaving the judgment to the court." (Code Civ. Proc., § 624.) In a case "[w]here a special finding of facts is inconsistent with the general verdict, the former controls the latter, and the court must give judgment accordingly." (Code Civ. Proc., § 625; see also *Tavaglione v. Billings* (1993) 4 Cal.4th 1150, 1156-1157; *Bond v. DeWitt* (1954) 126 Cal.App.2d 540, 544.)

The jury's findings that AIAC made representations recklessly but without knowing the statements were false are inherently inconsistent. A representation made recklessly without knowledge of its falsity is sufficient to establish scienter. (5 Witkin, Summary of Cal. Law (9th ed. 1988) Torts, § 705, p. 806.) However, on both fraud theories the jury found AIAC did not act with an intent to defraud plaintiff. An intent to induce reliance on a misrepresentation or nondisclosure by the plaintiff is essential to establish liability for either an intentional misrepresentation or concealment of a material fact. (*Lovejoy v. AT&T Corp.* (2001) 92 Cal.App.4th 85, 93; *Conrad v. Bank of America* (1996) 45 Cal.App.4th 133, 157; 5 Witkin, Summary of Cal. Law, *supra,* §§ 706, 710, pp. 807, 810.) The

absence of this element defeats plaintiff's fraud claim against AIAC. Furthermore, the finding relevant to defendants' punitive damages liability was in the nature of a general verdict and is subordinate to the jury's specific finding of no intent to defraud. Thus, the trial court properly entered judgment for AIAC on the fraud claim.

Plaintiff contends AIAC could be found liable either as a co-conspirator of National Union or on a theory of negligent misrepresentation. These contentions are without merit.

First, since plaintiff did not assert the latter theory at trial, and the court did not instruct the jury on it, it is now too late to do so. (*Overgaard v. Johnson* (1977) 68 Cal.App.3d 821, 826.) Second, while the court did instruct the jury on conspiracy as a basis for imposing liability, as plaintiff concedes the jury was not asked to return a special verdict on this allegation. Had the jury concluded AIAC was liable as a co-conspirator with National Union, it should have returned a finding of an intent to defraud.

A review of plaintiff's closing argument also reflects it relied on the representations and conduct of AIAC's employees, not conspiracy, to support its fraud claim. In fact, while discussing the question of whether National Union acted with malice, plaintiff's counsel suggested no conspiracy existed. "An insurance company whose job is to . . . investigate the situation thoroughly, concealing information which it knows is going to lead to a discovery that there's coverage – even concealing that information from its own claims people so that they won't have a guilty conscience about denying the claim – that's malice."

The trial court properly entered judgment for AIAC on the fraud claim.

The Brandt Damage Award

Plaintiff retained legal counsel under an agreement requiring it to pay counsel 40 percent of all amounts recovered in the case. After a lengthy discussion, the trial court limited the sum plaintiff could recover as damages under *Brandt v. Superior Court, supra,* 37 Cal.3d 813, to 40 percent of the amount recovered as policy benefits during the trial's first phase. Plaintiff attacks this ruling and claims it should have been allowed to recover the reasonable value of counsel's services which it calculates is nearly $300,000 greater than the amount awarded by trial court. This contention lacks merit.

Brandt held attorney fees reasonably incurred to compel payment of policy benefits tortiously withheld by an insurer are recoverable as an element of damages. (*Brandt v. Superior Court, supra,* 37 Cal.3d at pp. 815, 817.) "When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense. The attorney's fees are an economic loss – damages – proximately caused by the tort. [Citation.]" (*Id.* at p. 817.)

The retainer agreement required plaintiff to pay counsel 40 percent of all sums recovered in this action. It had no further legal obligation to pay counsel for the legal services rendered to it. *Brandt* expressly held the "fees recoverable . . . may not exceed the amount attributable to the attorney's efforts to obtain the rejected payment due on the insurance contract." (*Brandt v. Superior Court, supra,* 37 Cal.3d at p. 819.) Plaintiff cites no authority permitting a post-trial modification of the retainer agreement. Thus, the trial court did not err by limiting the

damage award under *Brandt v. Superior Court, supra,* 37 Cal.3d at p. 813 to the percentage specified in the parties' contingency agreement.

The Costs Award

Plaintiff attacks the trial court's postjudgment rulings concerning the award of costs on two grounds. Both arguments lack merit.

First, it disputes the court's finding AIAC was a prevailing party. Plaintiff argues that since National Union and AIAC filed a joint answer to the complaint and were represented by the same counsel during trial, they held a unity of interest which precludes AIAC from acquiring this status.

Code of Civil Procedure section 1032 defines prevailing party to include "a defendant in whose favor a dismissal is entered, a defendant where neither plaintiff nor defendant obtains any relief, and a defendant as against those plaintiffs who do not recover any relief against that defendant. . . . [I]n situations other than as specified, the 'prevailing party' shall be as determined by the court, and under those circumstances, the court, in its discretion, may allow costs or not and, if allowed may apportion costs between the parties on the same or adverse sides. . . . " (Code Civ. Proc., § 1032, subd. (a)(4).) In conformity with this statute, the case law holds that where only one of multiple, jointly-represented defendants presenting a unified defense prevails in an action, the trial court has discretion to award or deny costs to that party. (*Webber v. Inland Empire Investments, Inc.* (1999) 74 Cal.App.4th 884, 920; *Slavin v. Fink* (1994) 25 Cal.App.4th 722,

725-726; *Smith v. Circle P Ranch Co.* (1978) 87 Cal.App.3d 267, 272.)

Plaintiff asserts the trial court did not exercise its discretion in this case, citing a statement by the trial judge during the hearing on the motion to strike AIAC's cost bill. However, the court made that comment in response to plaintiff's contention "no evidence" exists "to support any particular allocation" between AIAC and National Union, and that the latter entity presumably "fronted" AIAC's trial expenses. The record as a whole does not support a conclusion the trial court failed to exercise its discretion concerning AIAC's status and its recovery of costs.

The related arguments also fail. Contrary to plaintiff's assertion this is not a case where it established wrongdoing against AIAC, but simply failed to recover a monetary award. The jury found AIAC did not commit fraud. Furthermore, since the injunctive relief claim had been previously dismissed, this was an action for damages. Thus, the evidence indicating AIAC subsequently modified its operating procedures concerning claims handling does not preclude it from being deemed a prevailing party.

Second, plaintiff contends the trial court erred by denying its recovery of expert witness fees under Code of Civil Procedure section 998. Nearly a year before trial, plaintiff served on National Union and AIAC an unsuccessful pretrial offer to compromise proposing "to allow judgment be taken . . . against defendants" for $626,489.26. In denying plaintiff's request for expert witness fees, the court cited *Taing v. Johnson Scaffolding Co.* (1992) 9 Cal.App.4th 579.

Code of Civil Procedure section 998, subdivision (d) authorizes the court to award a prevailing plaintiff its

expert witness fees if the plaintiff made timely pretrial offer to compromise which the defendant does not accept, and "the defendant fails to obtain a more favorable judgment. . . . " In *Taing,* the court reversed an award of costs, declaring "if a plaintiff elects to submit a section 998 offer in cases involving multiple defendants, the offer to any defendant against whom the plaintiff seeks to extract penalties for nonacceptance must be sufficiently specific to permit that individual defendant to determine the exact amount plaintiff is seeking from him or her." (*Taing v. Johnson Scaffolding Co., supra,* 9 Cal.App.4th at p. 586.) *Taing* explained its rule as follows: "[A]n unapportioned offer by a single plaintiff to multiple defendants . . . requires any defendant who wants to accept to obtain the concurrence of his or her codefendants. This places a reasonable defendant at the mercy of codefendants whose refusal to settle may be unreasonable." (*Id.* at p. 585.)

National Union and AIAC were not jointly and severally liable to plaintiff. (Cf. *Steinfeld v. Foote-Goldman Proctologic Medical Group, Inc.* (1996) 50 Cal.App.4th 1542, 1547-1549.) The complaint sought recovery against National Union on theories of breach of contract, bad faith, and fraud. AIAC was alleged to be liable only on the latter theory. Furthermore, the evidence relating to each defendant's liability for fraud was separate. Thus, the trial court did not err by exercising its discretion to deny recovery of expert witness fees in this case.

NATIONAL UNION'S APPEAL

Denial of an Offset

National Union moved to have the settlement amounts plaintiff received from Ferguson and TRM offset

against the damages plaintiff recovered from it. The trial court issued a lengthy written order denying the request as to both the contractual damages and the tort damages recovered by plaintiff. National Union contends the trial court erred by denying an offset in this case.

Consistent with the general rule imposing on a party the burden of proving the existence or nonexistence of each fact essential to a claim or defense (Evid. Code, § 500), "[a] defendant seeking an offset against a money judgment has the burden of proving the offset. [Citation.]" (*Conrad v. Ball Corp.* (1994) 24 Cal.App.4th 439, 444.)

With respect to plaintiff's contractual recovery, an insured is entitled to receive compensation in accordance with the policy terms, and an insurer cannot reduce the amount recoverable "merely because [the insured] has 'collateral contracts or relations with third persons which relieve him wholly or partly from the loss against which the insurance company agreed to indemnify him.' [Citations.]" (*Strickland v. Federal Ins. Co.* (1988) 200 Cal.App.3d 792, 801, quoting *Hughes v. Potomac Ins. Co.* (1962) 199 Cal.App.2d 239, 251, disapproved on another ground in *Sabella v. Wisler* (1963) 59 Cal.2d 21, 34.) An insurer's right to recoup payment of policy benefits is covered by the principle of subrogation. To qualify for subrogation, the insurer must pay the insured's loss. (*Sapiano v. Williamsburg Nat. Ins. Co.* (1994) 28 Cal.App.4th 533, 538; *Chase v. National Indemnity Co.* (1954) 129 Cal.App.2d 853, 861-862.)

National Union refused to pay any policy benefits to plaintiff. The cases on which it relies to establish an offset against the contract damages involve an insured's recovery of tort damages and whether the collateral source rule

applied. Its contention the trial court "misread" *Kardly v. State Farm Mut. Auto. Ins. Co.* (1989) 207 Cal.App.3d 479 is incorrect. Contrary to National Union's claim, *Kardly* did not hold the insurer waives the right of subrogation by breaching the insurance contract. The part of the *Kardly* opinion National Union quotes refers to the facts of another appellate decision. (*Id.* at p. 489.) Thus, the trial court properly refused to offset the Ferguson and TRM settlements against the contractual damage award.

As for plaintiff's recovery of tort damages, the trial court agreed the collateral source doctrine did not apply because Ferguson and TRM could not be deemed collateral sources under the facts of this case. However, the court detailed the potential liability facing Ferguson and TRM, and found their potential liability exceeded $261,000 which included nonduplicative exposure exceeding $96,000. Applying the tort of another doctrine, the court concluded the settlement sums paid by Ferguson and TRM should not be offset against plaintiff's recovery from National Union.

Generally, a party cannot obtain double recovery for the same wrong where joint or concurrent tortfeasors are jointly and severally liable for the same wrong. (6 Witkin, Summary of Cal. Law, *supra,* Torts, § 1322, at p. 779.) "[I]t has long been recognized that if one tortfeasor pays partial compensation to the plaintiff, the liability of other tortfeasors will be correspondingly reduced: ' . . . payments by one tortfeasor on account of a harm for which he and another are each liable, diminish the amount of the claim against the other whether or not it was so agreed at the time of payment and whether the payment was made before or after judgment. Since the plaintiff can have but one satisfaction, evidence of such payments is admissible for

the purpose of reducing pro tanto the amount of the damages he may be entitled to recover.' [Citations.]" (*Krusi v. Bear, Stearns & Co.* (1983) 144 Cal.App.3d 664, 673.)

Where tortious acts by separate persons produce the same indivisible injury, each person is liable for the whole loss even if they did not act in concert. (*Sanchez v. Bay General Hospital* (1981) 116 Cal.App.3d 776, 796.) Thus, while plaintiff sued National Union for breach of contract, breach of the implied covenant of good faith and fair dealing, and fraud, but only sought damages against Ferguson and TRM for negligence, the injury it suffered was the same.

However, the court did find the tort of another doctrine applicable to this case. "A person who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover compensation for the reasonably necessary loss of time, attorney's fees, and other expenditures thereby suffered or incurred. [Citations.]" (*Prentice v. North Amer. Title Guar. Corp.* (1963) 59 Cal.2d 618, 620.)

Generally, a party seeking to recover litigation costs under this rule must plead and prove the claim. (*Hsu v. Abbara* (1995) 9 Cal.4th 863, 869, fn. 4.) While plaintiff did not do so here, the potential for its recovery of damages from Ferguson and TRM was made known to them during pretrial discovery. Furthermore, had it not settled with Ferguson and TRM, plaintiff could have amended the complaint to assert its right to recover the fees and expenses incurred in its action against National Union.

The record supports the trial court's denial of National Union's request for an offset.

PUNITIVE DAMAGES

Introduction

Both parties attack the punitive damage award. National Union challenges the sufficiency of the evidence supporting the recovery of exemplary damages, the court's refusal to instruct the jury National Union could only be subject to punitive damages based on its own employees' conduct, and the constitutionality of the award imposed on it. Plaintiff contends the trial court erred by reducing the punitive damage award to $1.7 million.

Sufficiency of the Evidence

National Union claims its own conduct was not oppressive, fraudulent, or malicious, TRM's activity cannot be attributed to it, and it did not ratify TRM's actions.

Civil Code section 3294 authorizes the award of punitive damages in any "action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice. . . . " (Civ. Code, § 3294, subd. (a).) In *Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, the Supreme Court upheld an award of punitive damages against an insurer based on evidence two employees, a claims manager and a claims adjuster, failed to adequately investigate the insured's claims under a disability insurance policy. "The determination whether employees act in a managerial capacity, however, does not necessarily hinge on their 'level' in the corporate hierarchy. Rather, the critical inquiry is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy. When employees dispose of insureds' claims with little if any supervision, they possess

sufficient discretion for the law to impute their actions concerning those claims to the corporation." (*Id.* at pp. 822-823.)

Subsequently, the Legislature amended Civil Code section 3294 to provide, "[a]n employer shall not be liable for [punitive] damages . . . based upon acts of an employee of the employer, unless the employer had advance knowledge of the unfitness of the employee and employed him or her with a conscious disregard of the rights or safety of others or authorized or ratified the wrongful conduct for which the damages are awarded or was personally guilty of oppression, fraud, or malice. With respect to a corporate employer, the advance knowledge and conscious disregard, authorization, ratification or act of oppression, fraud, or malice must be on the part of an officer, director, or managing agent of the corporation." (Civ.Code, § 3294, subd. (b).)

In *White v. Ultramar, Inc.* (1999) 21 Cal.4th 563, the Supreme Court considered the effect of this amendment in an action for wrongful termination. A manager who was responsible for eight stores, covering sixty-five employees, had fired the plaintiff, a convenience store employee. The jury awarded plaintiff both compensatory and punitive damages.

In affirming, the Supreme Court concluded that "in amending section 3294, the Legislature intended (like *Egan, supra,* 24 Cal.3d at p. 823) to limit corporate punitive damage liability to those employees who exercise substantial independent authority and judgment over decisions that ultimately determine corporate policy." (*White v. Ultramar, Inc., supra,* 21 Cal.4th at p. 573.) The

court noted "section 3294, subdivision (b), placed ['managing agent'] next to the terms 'officer' and 'director,' intending that a managing agent be more than a mere supervisory employee. The managing agent must be someone who exercises substantial discretionary authority over decisions that ultimately determine corporate policy. Thus, by selecting the term 'managing agent,' and placing it in the same category as 'officer' and 'director,' the Legislature intended to limit the class of employees whose exercise of discretion could result in a corporate employer's liability for punitive damages." (*Ibid.*) The critical factor "'" . . . is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy." [Citation.]'" (*Id.* at p. 573.)

The agency agreement between National Union and TRM and the evidence in this case shows TRM had broad discretion over National Union's bus insurance program. TRM could "solicit, bind, write and administer insurance" policies, and "exercise [its] independent judgment as to the time, place and manner of soliciting insurance and servicing policyholders." There was evidence AIAC directed its employees to contact TRM when seeking coverage verification. In this case, TRM participated in issuing the policy to Ko, in subsequently canceling it, and then reinstating a modified version of it. Later, when Ko submitted a claim on the bus, TRM initially issued a coverage determination, but then prepared an endorsement deleting the vehicle from the policy, and advised AIAC to deny the claim. Furthermore, TRM's president was in contact with both AIAC and the senior management of the division handling National Union's bus program when plaintiff's claim was being considered, and participated in the ultimate decision to deny it. This evidence supports the jury's conclusion

TRM was National Union's managing agent, thereby subjecting it to punitive damages under Civil Code section 3294. (*White v. Ultramar, Inc., supra,* 21 Cal.4th at p. 577; *Egan v. Mutual of Omaha Ins. Co., supra,* 24 Cal.3d at p. 823.)

In light of this conclusion it is unnecessary to consider National Union's additional claims concerning instructional error and alleged insufficiency of the evidence based on its own conduct.

Validity of the Trial Court's Remittitur

The trial court issued a post-judgment order conditionally granting National Union a new trial on the insurance bad faith and fraud counts and on plaintiff's right to receive punitive damages unless the latter agreed to reduce the punitive damage award to $1.7 million. Plaintiff timely consented to the remittitur. After National Union filed its appeal, plaintiff cross-appealed and now challenges the remittitur's validity.

A trial court has the discretion to conditionally grant a new trial unless the plaintiff consents to a reduction of a damages award where the court independently determines the jury's award is excessive. (Code Civ. Proc., § 662.5, subd. (b); *Schelbauer v. Butler Manufacturing Co.* (1984) 35 Cal.3d 442, 452-453; *West v. Johnson & Johnson Products, Inc.* (1985) 174 Cal.App.3d 831, 876.) Reversal of the ruling is allowed only where there is no substantial basis in the record to support the reasons articulated by the trial court for its decision. (Code Civ. Proc., § 657; *Jahn v. Brickey* (1985) 168 Cal.App.3d 399, 408.)

The court noted the ratio of the original punitive damage award to compensatory damages (60 to 1) created a presumption the jury's verdict was the result of passion and prejudice. (*Rosener v. Sears, Roebuck & Co.* (1980) 110 Cal.App.3d 740, 752.) Plaintiff focuses much its argument on the reprehensible nature of National Union's conduct. While the court agreed the evidence supported the jury's conclusion National Union had acted reprehensibly, it concluded the jury had placed too much emphasis on National Union's financial wealth and failed to adequately consider the relationship between the injury suffered by plaintiff and the amount of the punitive damage award. The court noted this lawsuit involves an action by one corporate entity against another corporate entity to recover only for economic loss, the value of plaintiff's security interest in a damaged bus. Given these circumstances, the trial court noted upholding the original award raised serious constitutional concerns.

Plaintiff also challenges the portion of the remittitur order requiring it to choose between a reduction in punitive damages and a new trial on *both* liability and the amount of punitive damages. In so ruling, the trial court cited *Medo v. Superior Court* (1988) 205 Cal.App.3d 64. Plaintiff relies on *Torres v. Automobile Club of So. California* (1997) 15 Cal.4th 771 in challenging the trial court's ruling.

Torres held Civil Code section 3295, subdivision (d) did not require an *appellate* court which reverses an excessive punitive damage award to order a new trial on all issues, including liability and the amount of compensatory damages. (*Id.* at pp. 777-781.) In so ruling, *Torres* distinguished *Medo*. (*Id.* at p. 780.) In *Medo*, the *trial* court ordered a new trial on all issues when the jury was

discharged after completion of the liability phase. While agreeing with the plaintiffs' assertion that the defendants had waived their right to have the same jury determine both liability and the right to punitive damages, the appellate court nonetheless noted, "[p]unitive damages are not simply recoverable in the abstract. They must be tied to oppression, fraud or malice *in the conduct which gave rise to liability in the case.* Thus . . . , the instruction on punitive damages[ ] tells the jury that in arriving at an award of punitive damages, it is to consider the reprehensibility of the conduct of the defendant and that the punitive damages must bear a reasonable relation to the actual damages. In order for a jury to evaluate the oppression, fraud or malice in the conduct giving rise to liability in the case, it must consider the conduct giving rise to liability." (*Medo v. Superior Court, supra,* 205 Cal.App.3d at p. 68.)

However, even assuming the trial court erred by relying on *Medo* to order a new trial on all issues if plaintiff refused to accept a reduction in the punitive damage award, the ruling does not require reversal. As the trial judge concluded, the jury's $10 million punitive damage award was clearly constitutionally suspect. Thus, ordering a remittitur in this case was appropriate under the circumstances.

Validity of the Award

Finally, National Union contends even the $1.7 million punitive damage award is unconstitutional and excessive. In our original opinion, we upheld the award under a deferential standard of review. The United States Supreme Court vacated the original judgment and

directed us to review the punitive damage award's constitutional validity under the independent review standard enunciated in *Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. 424.

The Supreme Court has declared, "the broad discretion" possessed by the states "with respect to the imposition of . . . punitive damages," is limited by the Constitution's Due Process Clause which "prohibits the States from imposing 'grossly excessive' punishments on tortfeasors . . . [citations]." (*Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at pp. 433-434.) In determining whether the punitive damage award in a particular case is "'grossly disproportional' to the gravity of [defendants'] offense[s]'" (*Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at p. 434), a reviewing court must consider "[t]hree guideposts": "[T]he degree of reprehensibility [of the wrongdoer's conduct]; the disparity between the harm or potential harm suffered . . . and [the] punitive damages award; and the difference between this remedy and the civil penalties authorized or imposed in comparable cases." (*BMW of North America, Inc. v. Gore* (1996) 517 U.S. 559, 574-575; see also *Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at p. 435.) On appeal, a reviewing court considering a constitutional challenge to a punitive damage award must conduct a "thorough, independent review" of the award. (*Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at p. 441.)

The bulk of National Union's argument focuses on the reprehensibility factor. The evidence clearly reflects reprehensible conduct occurred in this case. To the extent National Union suggests Textron was not subjected to any oppression, fraud, or malice, *Cooper Industries* recognizes

that, in making an independent determination on the constitutionality of a punitive damage award, an appellate court "should defer to the [trial court's] findings of fact unless they are clearly erroneous. [Citation.]" (*Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at p. 440, fn. 14.) Here, the evidence supports the jury and trial court's finding of the predicate fact required for imposing exemplary damages.

National Union argues TRM, not it, committed the wrongdoing and its liability for TRM's actions is merely vicarious. But as discussed above, TRM "exercise[d] substantial discretionary authority over decisions . . . ultimately determin[ing] corporate policy" for the bus insurance program (*White v. Ultramar, Inc., supra,* 21 Cal.4th at p. 573), and thus constituted National Union's managing agent. Simply describing National Union's liability as vicarious does not militate against imposing a proportionately appropriate punitive damage award against it based on TRM's wrongdoing.

National Union also claims that "at most [it] failed to properly investigate TRM's conduct, and was not itself involved in the scheme to manufacture documents to conceal the existence of coverage." We reject the proposition that, to limit or avoid liability for exemplary damages, a principal may rely on its own self-imposed ignorance of a managing agent's wrongdoing. National Union further contends the reprehensibility factor does not support the punitive damage award because the injury suffered was only economic in nature. But the Supreme Court has recognized "infliction of economic injury, especially when done intentionally through affirmative acts of misconduct, [citation] . . . can warrant a substantial penalty." (*BMW of North America, Inc. v. Gore, supra,* 517 U.S. at p. 576.)

The second "guidepost[ ]" relevant to the constitutional validity of the punitive damage award is "the disparity between the harm or potential harm suffered . . . and [the] punitive damages award. . . . " (*BMW of North America, Inc. v. Gore, supra,* 517 U.S. at p. 575.) Here, Textron recovered compensatory damages exceeding $165,000. Thus, the ratio between the actual harm caused by National Union and the trial court's reduced punitive damage award of $1.7 million is roughly 10 to 1.

National Union claims the ratio between compensatory damages and punitive damages should not exceed 4 to 1, and thus, the 10 to 1 ratio in this case is constitutionally impermissible. We disagree. *BMW of North America, Inc. v. Gore, supra,* 517 U.S. 559 declared, "we have consistently rejected the notion that the constitutional line is marked by a simple mathematical formula. . . . " (*Id.* at p. 582.) In a passage relevant to the present case, the Court emphasized this point by noting, "low awards of compensatory damages may properly support a higher ratio than high compensatory awards, if, for example, a particularly egregious act has resulted in only a small amount of economic damages." (*Ibid.*) While the compensatory award in this case was modest, in light of the reprehensible conduct attributable to National Union, the trial court properly imposed a punitive damage award sufficiently high to achieve the twin objectives of punishment and deterrence.

The third "guidepost[ ]" concerns a comparison of "the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct. . . . " (*BMW of North America, Inc. v. Gore, supra,* 517 U.S. at p. 583.) National Union notes the Insurance Code only imposes fines of between $10,000 and $55,000 for

misconduct by insurers. However, Textron notes Penal Code section 550, subdivision (b) makes it a felony subject to fine or imprisonment to "knowingly assist or conspire with any person to" either "[p]resent" or "[p]repare" a "written . . . statement . . . in . . . opposition to [ ] a claim" for insurance benefits, or to "[c]onceal, or . . . fail to disclose the occurrence of [ ] an event that affects any person's initial or continued right or entitlement to any insurance benefit or payment. . . . " (Pen. Code, § 550, subd. (b)(1), (2) & (3).) Furthermore, the focus of an analysis of a punitive damage award's constitutionality is to ensure the wrongdoer "receive[s] fair notice not only of the conduct that will subject him to punishment, but also of the severity of the penalty that a State may impose." (*BMW of North America, Inc. v. Gore, supra,* 517 U.S. at p. 574, fn. omitted.) In reversing the award in *Gore,* the Supreme Court noted "there does not appear to have been any judicial decision in Alabama or elsewhere indicating [the defendant's wrongful activity] might give rise to such severe punishment." (*Id.* at p. 584.) Here, the same cannot be said to be true. It has long been common knowledge acts of bad faith by insurers could subject that party to significant punitive damage awards. (See *Neal v. Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 928-929.)

Thus, we conclude that, even under a de novo review, the $1.7 million punitive damage award in this case does not violate National Union's constitutional right to due process of law.

As for the excessiveness of the punitive damage award under state law, "[t]he California Supreme Court has established three criteria for making that determination: (1) the reprehensibility of the defendant's misdeeds; (2) the amount of compensatory damages, though there is no fixed ratio for determining whether punitive damages are

reasonable in relation to actual damages; and (3) the defendant's financial condition. [Citations.]" (*Stevens v. Owens-Corning Fiberglas Corp.* (1996) 49 Cal.App.4th 1645, 1658.) On appeal, the award is presumed to be correct and will be reversed only if the record, viewed most favorably to the judgment, reflects the award is the result of passion or prejudice. (*Ibid.*)

Our foregoing discussion of the reprehensibility and ratio criteria is equally applicable in this context and need not be repeated. As for the third factor, "[t]he wealthier the wrongdoer, the larger the punitive damage award must be to meet the goals of punishment and deterrence. [Citations.]" (*Stevens v. Owens-Corning Fiberglas Corp., supra,* 49 Cal.App.4th at p. 1658.) Consequently, to enforce the purposes of punishing the wrongdoer and deterring similar future wrongful conduct (*Cooper Industries, Inc. v. Leatherman Tool Group, Inc., supra,* 532 U.S. at p. 432; *PPG Industries, Inc. v. Transamerica Ins. Co.* (1999) 20 Cal.4th 310, 317), the award necessarily had to be large enough to affect a corporate entity such as National Union. We conclude the punitive damage award is not excessive under California law.

DISPOSITION

The judgment and postjudgment orders are affirmed. Each party shall bear its own costs on appeal.

RYLAARSDAM, J.

WE CONCUR:

SILLS, P. J.

O'LEARY, J.

COPY

NOT TO BE PUBLISHED

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORPORATION, Plaintiff and Appellant, v. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA et al., Defendants and Appellants.	G020323 (Super. Ct. No. 734096) OPINION (Filed Jan. 29, 2001)

Appeals from a judgment and post-judgment orders of the Superior Court of California, County of Orange, Nancy Wieben Stock and Raymond J. Ikola, Judges. Motion to Augment the record on appeal. Judgment and post-judgment orders affirmed. Motion granted.

Albert Weiland & Golden and Marcus M. Kaufman; Stephan, Oringher, Richman & Theodora and Robert M. Dato for Plaintiff and Appellant.

Horvitz & Levy, Mitchell C. Tilner and Peter Abrahams; Lewis, D'Amato, Brisbois & Bisgaard, R. Gaylord Smith and Michael W. Connally for Defendants and Appellants.

* * *

Plaintiff Textron Financial Corporation sued defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union) and others over a refusal to honor a claim for insurance benefits concerning property damage to a commercial bus in which it held a security interest. Plaintiff settled with two parties and proceeded to trial against National Union and American International Adjustment Company, Inc. (AIAC), National Union's claims adjuster. After a lengthy trial divided into three phases, the trial court entered judgment on a jury's special verdict awarding plaintiff $165,414.40 in compensatory damages and $10 million in punitive damages against National Union. The court entered judgment, including costs, for AIAC against plaintiff.

Both plaintiff and National Union filed post-judgment motions. The trial court denied National Union's motion for judgment notwithstanding the verdict and plaintiff's motion for new trial, but conditionally granted National Union a new trial unless plaintiff agreed to reduce the punitive damage award to $1.7 million. Plaintiff agreed to the remittitur. The court also struck plaintiff's request for expert witness fees.

National Union appeals from the judgment and the denial of its motion for judgment notwithstanding the verdict, challenging both the punitive damage award on several grounds, and the trial court's refusal to offset the amounts plaintiff received in the pre-trial settlements. Plaintiff appeals, challenging the trial court's striking of its cause of action for unfair business practices, the judgment in favor of AIAC, including costs, the remittitur of punitive damages, and the denial of its request for expert witness fees.

FACTS

Il Sung Ko operated a tour bus company, Taeguk Tour and Sightseeing (Taeguk). Plaintiff loaned Ko funds to purchase a bus, receiving in return a security interest in the vehicle. The security agreement required Ko to insure the bus. Ko obtained a National Union liability insurance policy through D.W. Ferguson & Associates, Inc. (Ferguson), an independent insurance brokerage. The policy was issued through TRM International, Inc. (TRM), a company appointed by National Union to solicit, bind, write, and administer policies for its commercial bus program. The policy listed plaintiff as a loss payee and required National Union to mail plaintiff notice in advance if it cancelled the policy.

Taeguk suffered a downturn in business and Ko failed to timely pay his insurance premiums. In October 1992, TRM sent Ko notice it intended to cancel the policy. TRM did not send a copy of the cancellation notice to plaintiff. The policy terminated November 27.

Beginning in late October and throughout November, Ferguson and Taeguk discussed reducing the insurance premiums by deleting coverage for some of Ko's vehicles. Ferguson also corresponded with a TRM underwriter about the situation, proposing the issuance of a new policy covering only some of Ko's busses. The underwriter suggested an alternative whereby TRM would reinstate the original policy and give Ko a credit against his policy's premium if he agreed to certain conditions, which included delivering the license plates of two buses to Ferguson and temporarily suspending use of those vehicles. Plaintiff presented expert testimony that, unlike a transaction where a vehicle is deleted from a policy, the alternative

approach implemented a procedure described as lay-up credit. Under a lay-up credit, the insured maintains coverage on a vehicle while it is not being operated.

Ko agreed to this proposal, and on December 1, TRM reinstated the policy effective as of November 27. The bus encumbered by plaintiff's security interest was one of the vehicles Ko intended not to use. Plaintiff did not receive notice of the policy reinstatement with the endorsement which reflected Ko's business received a premium credit due to the vehicle's non-use. National Union claimed it sent a copy of this endorsement to plaintiff, but plaintiff denied receiving it.

In January 1993, the bus encumbered by plaintiff's lien suffered extensive damage when it collided with another vehicle on a public highway. At Taeguk's request, Ferguson submitted a notice of claim to AIAC. On February 4, TRM sent AIAC a notice verifying coverage for the vehicle and confirming plaintiff as a loss payee. However, after further correspondence with Taeguk and TRM, AIAC denied the claim, asserting the bus had been deleted from the policy before the accident. TRM prepared an endorsement deleting the bus from the policy (Number 8) on February 16. This endorsement purported to be effective as of December 1, 1992.

In late 1993, Ko defaulted on plaintiff's loan. Plaintiff then learned about the accident and contacted Ferguson concerning insurance benefits to repair the vehicle. Ferguson informed plaintiff the bus had been removed from the policy before the accident. Plaintiff sued Ko, recovering a judgment against him and incurring $3,859.50 in legal fees in the process. However, Ko filed bankruptcy and discharged the debt.

Plaintiff submitted a claim to National Union for benefits under the insurance policy. At that time, it possessed only a certificate of insurance, not a copy of the policy.

AIAC also handled plaintiff's claim. TRM informed AIAC the encumbered bus had been deleted from the policy before the accident and sent it a copy of endorsement number 8. A certificate of mailing on that copy covered the part of the endorsement reflecting the date TRM had prepared it. After an AIAC claims manager discussed the matter with John Lavin, a senior underwriter with the division handling National Union's bus program, and Tom Spangenberg, TRM's president, AIAC advised plaintiff the claim was being denied. The basis of the denial was that Ko deleted the bus from the policy before the accident, and TRM and AIAC concluded National Union's policy did not obligate it to give plaintiff advance notice of the deletion. National Union did not send plaintiff a copy of the policy until August 1994. Again, the portion of endorsement Number 8 displaying the date on which it had been prepared was covered by the mailing certificate.

PROCEDURAL BACKGROUND

The trial's first phase dealt with plaintiff's breach of contract claim against National Union. The court found, as a matter of law, the insurance contract's loss-payable clause constituted a separate agreement between plaintiff and National Union, obligating National Union to provide 30 days' notice of the policy's cancellation or the bus's deletion from it, and that National Union failed to comply with this requirement. The jury subsequently returned a

special verdict awarding plaintiff $61,513.80 under the policy.

The second phase involved plaintiff's causes of action for bad faith against National Union and fraud against both National Union and AIAC. The jury returned a special verdict finding National Union violated the policy's implied covenant of good faith and fair dealing and that it acted with oppression, malice, and fraud in doing so. The jury also returned a special verdict, finding National Union liable for intentional misrepresentation and concealment, and awarded plaintiff $3,859.80 in damages. Based on its interpretation of the jury's answers in the special verdict, the trial court entered judgment for AIAC on the fraud count.

During this phase, the trial court also ruled plaintiff could recover $30,268.16 in attorney fees as damages under *Brandt v. Superior Court* (1985) 37 Cal.3d 813. The parties stipulated plaintiff was entitled to $55,616.34 in costs pursuant to *Brandt*. Subsequently, the court denied National Union's request to offset the pretrial settlements plaintiff received from Ferguson ($26,500) and TRM ($62,500) against the compensatory award imposed on it.

The trial's third phase dealt with punitive damages. The jury returned a special verdict assessing $10 million in punitive damages against National Union which the trial court subsequently reduced to $1.7 million. In addition, the judgment awarded plaintiff compensatory damages, consisting of the policy benefits plus interest, the legal expenses recoverable under *Brandt v. Superior Court, supra,* 37 Cal.3d 813, and the damages for fraud. Finally, the court awarded AIAC $10,277.52 in costs against plaintiff.

DISCUSSION

PLAINTIFF'S APPEAL

Demurrer to the Unfair Business Practices Cause of Action

The complaint's fourth count sought injunctive and restitutionary relief under Business and Professions Code section 17200 et seq. against National Union and AIAC for "engag[ing] in unfair competition" in "handling [of plaintiff's] claim, and the claims of other persons." Plaintiff alleged National Union, "aided and abetted" by AIAC, "used misleading documents to falsely suggest that it would provide insurance . . . where it had no intention to do so," and "falsely suggested that it would . . . provid[e] timely notice of [policy] cancellations," "misrepresented the terms and meaning of its policies . . . to provide a pretext for its refusal to provide timely notice," and "engaged in a pattern and practice of wrongful and false cancellations of insurance policies. . . . "

Relying on *Moradi-Shalal v. Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, National Union and AIAC generally demurred to this count. The trial court sustained the demurrers without leave to amend. Citing *State Farm Fire & Casualty Co. v. Superior Court* (1996) 45 Cal.App.4th 1093, plaintiff contends the trial court's ruling was erroneous.

Moradi-Shalal held the Unfair Insurance Practices Act (Ins.Code, § 790 et seq.; UIPA) does not create a private cause of action against insurers who violate its provisions. (*Moradi-Shalal v. Fireman's Fund Ins. Companies, supra,* 46 Cal.3d at pp. 304-305.) This rule applies to both first party and third party claims. (*Maler v. Superior Court* (1990) 220 Cal.App.3d 1592, 1597-1598; *Zephyr*

Park v. Superior Court (1989) 213 Cal.App.3d 833, 836-838.) While insurance companies are subject to California laws generally applicable to other businesses, including laws governing unfair business practices (Ins.Code, § 1861.03, subd. (a)), parties cannot plead around *Moradi-Shalal's* holding by merely relabeling their cause of action as one for unfair competition. (*Manufacturers Life Ins. Co. v. Superior Court* (1995) 10 Cal.4th 257, 283-284; *Maler v. Superior Court, supra,* 220 Cal.App.3d at p. 1598; *Safeco Ins. Co. v. Superior Court* (1990) 216 Cal.App.3d 1491, 1494.)

The specific allegations of wrongful conduct contained in plaintiff's fourth cause of action, using misleading documents and misrepresenting both the terms of the insurance policies and its obligations under them for its own benefit, are the type of activities covered by the UIPA. (Ins.Code, § 790.03, subds. (a) & (h).) In *Safeco Ins. Co. v. Superior Court, supra,* 216 Cal.App.3d 1491, the court ordered dismissal of an action which included a request for injunctive relief under Business and Professions Code section 17200 et seq. based on an insurer's allegedly unfair claims settlement practices. (*Id.* at pp. 1493-1494.) "Though the issue is one of first impression, we have no difficulty in deciding the Business and Professions Code provides no toehold for scaling the barrier of *Moradi-Shalal*. . . . To permit plaintiff to maintain this action would render *Moradi-Shalal* meaningless." (*Id.* at p. 1494.) Under the foregoing cases, merely alleging these purported acts constitute unfair business practices under the unfair competition law is insufficient to overcome *Moradi-Shalal.*

In a few cases, the Supreme Court has allowed an action against an insurance company under the unfair

competition law where the alleged conduct constituted an unlawful restraint on trade under the Cartwright Act (Bus. & Prof. Code, § 16700 et seq.), even though it also violated the UIPA. (*Quelimane Co. v. Stewart Title Guarantee Co.* (1998) 19 Cal.4th 26, 43-44; *Manufacturers Life Ins. Co. v. Superior Court, supra,* 10 Cal.4th at pp. 283-284.) "This conclusion does not compromise the rule of *Moradi-Shalal* in any way. The court concluded there that the Legislature did not intend to create new causes of action when it described unlawful insurance business practices in section 790.03, and therefore that section did not create a private cause of action under the UIPA. The court did not hold that by identifying practices that are unlawful in the insurance industry, practices that violate the Cartwright Act, the Legislature intended to bar Cartwright Act causes of action based on those practices." (*Manufacturers Life Ins. Co. v. Superior Court, supra,* 10 Cal.4th at p. 284.)

The case on which plaintiff relies, *State Farm Fire & Casualty Co. v. Superior Court, supra,* 45 Cal.App.4th 1093, held the plaintiff-insureds had sufficiently alleged a cause of action against their insurer under the unfair competition law based on allegations of conduct constituting common law fraud and breach of the implied covenant of good faith and fair dealing, even though the same conduct violated the UIPA. "While *Moradi-Shalal* clearly held that the Legislature did not intend to create new causes of action when it enacted section 790.03, it is also clear that the Legislature did not intend in any way to circumscribe the previously existing common law right of an insured to seek redress for an insurer's fraudulent deception or breach of the covenant of good faith implied in the policy. . . . Thus, . . . common law claims remain as a

firm legal basis on which an insured may rely to seek redress against an insurer." (*Id.* at pp. 1107-1108.)

The persuasiveness of *State Farm* has been undercut by the Supreme Court's subsequent disapproval of its definition of "unfair" business practices. Quoting from *People v. Casa Blanca Convalescent Homes, Inc.* (1984) 159 Cal.App.3d 509, *State Farm* declared: "The test of whether a business practice is unfair 'involves an examination of [that practice's] impact on its alleged victim, balanced against the reasons, justifications and motives of the alleged wrongdoer. In brief, the court must weigh the utility of the defendant's conduct against the gravity of the harm to the alleged victim. . . . [Citations.]'. . . . [A]n 'unfair' business practice occurs when that practice 'offends an established public policy or when the practice is immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers.' [Citation.]" (*State Farm Fire & Casualty Co. v. Superior Court, supra,* 45 Cal.App.4th at pp. 1103-1104, fn. omitted.)

In *Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.* (1999) 20 Cal.4th 163, the Supreme Court found this definition "too amorphous and provid[ing] too little guidance to courts and businesses." (*Id.* at pp. 184-185.) While *Cel-Tech Communications* limited its discussion to the context of an action between competitors, the court concluded, "any finding of unfairness to competitors under section 17200 be tethered to some legislatively declared policy or proof of some actual or threatened impact on competition," and that under Business and Professions Code section 17200, "the word 'unfair' . . . means conduct that threatens an incipient violation of an antitrust law, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a

violation of the law. . . . " (*Id.* at pp. 186-187, fn. omitted. See *Schnall v. Hertz Corp.* (2000) 78 Cal.App.4th 1144, 1165-1167 [applying *Cel-Tech Communications, Inc.'s* standard in vehicle lessee's action against rental agency for allegedly concealing or obscuring the rental agreement's fuel service charge].)

Harmonizing *Moradi-Shalal's* holding with the foregoing decisions supports a conclusion the trial court properly sustained the demurrers to plaintiff's unfair competition claim. First, the holding in *Safeco Ins. Co. v. Superior Court, supra,* 216 Cal.App.3d 1491 supports this result. Second, this case is distinguishable from *Quelimane* and *Manufacturers Life* in two respects. Neither decision involved an action by an insured or a third party based on the insurer's alleged failure to comply with a policy or to provide benefits. In *Quelimane,* parties who acquired real estate at tax sales sued title insurance companies for refusing to issue policies on their property. *Manufacturers Life* concerned an insurance agency's action against insurance companies for boycotting the agency. Also, in both cases the plaintiff alleged a Cartwright Act violation as the basis for its unfair competition cause of action. Finally, given the Supreme Court's disapproval of *State Farm's* "amorphous" definition of "unfair" practices and its focus on legislatively declared public policy, reliance on general common law principles to support a cause of action for unfair competition is unavailing.

Under these circumstances, the trial court properly found plaintiff failed to state a cause of action against National Union and AIAC for unfair business practices.

The Jury's Phase Two Findings

During the second phase, the jury returned a special verdict containing findings on the elements of two theories of deceit, intentional misrepresentation and concealment of a material fact. The jury's responses reflect it found both National Union and AIAC made representations of a material fact on which plaintiff justifiably relied to its injury, and that both defendants made the representations "recklessly without knowing whether [they were] true or false." However, the jury concluded AIAC did not know the representations were false, and did not make them with the intent to defraud plaintiff. On the concealment theory, the jury found both defendants concealed or suppressed a material fact which resulted in injury to plaintiff, but also found AIAC did not intentionally conceal or suppress a material fact with the intent to defraud plaintiff. In addition, the jury concluded both defendants were "guilty of fraud, malice, or oppression in the conduct upon which [it] based [its] finding of liability. . . ."

When the jury returned its special verdict, the court discussed the inconsistency in the findings with counsel, and ultimately ruled AIAC "is not liable for fraud or concealment." Plaintiff argues the trial court erred by construing the jury's findings to exonerate AIAC.

The distinction between a general verdict and a special verdict is that under the former a jury "pronounce[s] generally upon all or any of the issues," while the latter is one "by which the jury find the facts only, leaving the judgment to the court." (Code Civ. Proc., § 624.) In a case "[w]here a special finding of facts is inconsistent with the general verdict, the former controls the latter, and the court must give judgment accordingly." (Code Civ.

Proc., § 625; see also *Tavaglione v. Billings* (1993) 4 Cal.4th 1150, 1156-1157; *Bond v. DeWitt* (1954) 126 Cal.App.2d 540, 544.)

The jury's findings that AIAC made representations recklessly but without knowing the statements were false are inherently inconsistent. A representation made recklessly without knowledge of its falsity is sufficient to establish scienter. (5 Witkin, Summary of Cal. Law (9th ed. 1988) Torts, § 705, p. 806.) However, on both fraud theories the jury found AIAC did not act with an intent to defraud plaintiff. An intent to induce a particular act by the plaintiff is essential to establish liability for either an intentional misrepresentation or concealment of a material fact. (*Conrad v. Bank of America* (1996) 45 Cal.App.4th 133, 157; 5 Witkin, Summary of Cal. Law, *supra*, §§ 706 & 710, pp. 807, 810.) The absence of this element defeats plaintiff's fraud claim against AIAC. Furthermore, the finding relevant to defendants' punitive damages liability was in the nature of a general verdict and is subordinate to the jury's specific finding of no intent to defraud. Thus, the trial court properly entered judgment for AIAC on the fraud claim.

Plaintiff contends AIAC could be found liable either as a co-conspirator of National Union or on a theory of negligent misrepresentation. These contentions are without merit.

First, since plaintiff did not assert the latter theory at trial, and the court did not instruct the jury on it, it is now too late to do so. (*Overgaard v. Johnson* (1977) 68 Cal.App.3d 821, 826.) Second, while the court did instruct the jury on conspiracy as a basis for imposing liability, as plaintiff concedes, the jury was not asked to return a

special verdict on this allegation. Had the jury concluded AIAC was liable as a co-conspirator with National Union, it should have returned a finding of an intent to defraud.

A review of plaintiff's closing argument also reflects it relied on the representations and conduct of AIAC's employees, not conspiracy, to support its fraud claim. In fact, while discussing the question of whether National Union acted with malice, plaintiff's counsel suggested no conspiracy existed. "An insurance company whose job is to . . . investigate the situation thoroughly, concealing information which it knows is going to lead to a discovery that there's coverage – even concealing that information from its own claims people so that they won't have a guilty conscience about denying the claim – that's malice."

The trial court properly entered judgment for AIAC on the fraud claim.

The Attorney Fees Damage Award

Plaintiff retained legal counsel under an agreement requiring it to pay counsel 40 percent of all amounts recovered in the case. After a lengthy discussion, the trial court limited the attorney fees plaintiff could recover as damages under *Brandt v. Superior Court, supra,* 37 Cal.3d 813, to 40 percent of the amount recovered as policy benefits during the trial's first phase. Plaintiff attacks this ruling and claims it should have been allowed to recover the reasonable value of counsel's services which it calculates is nearly $300,000 greater than the amount awarded by trial court. This contention lacks merit.

Brandt held attorney fees reasonably incurred to compel payment of policy benefits tortiously withheld by

an insurer are recoverable as an element of damages. (*Brandt v. Superior Court, supra,* 37 Cal.3d at pp. 815, 817.) "When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense. The attorney's fees are an economic loss – damages – proximately caused by the tort. [Citation.]" (*Id.* at p. 817.)

The retainer agreement required plaintiff to pay counsel 40 percent of all sums recovered in this action. It had no further legal obligation to pay counsel for the legal services rendered to it. *Brandt* expressly held the "fees recoverable . . . may not exceed the amount attributable to the attorney's efforts to obtain the rejected payment due on the insurance contract." (*Brandt v. Superior Court, supra,* 37 Cal.3d at p. 819.) Plaintiff cites no authority permitting a post-trial modification of the retainer agreement. Thus, the trial court did not err by limiting the attorney fee damage award to the percentage specified in the parties' contingency agreement.

The Post-Judgment Costs Award

Plaintiff attacks the trial court's post-judgment rulings concerning the award of costs on two grounds. Both arguments lack merit.

First, it disputes the court's finding AIAC was a prevailing party. Plaintiff argues that since National Union and AIAC filed a joint answer to the complaint and were represented by the same counsel during trial, they held a unity of interest which precludes AIAC from acquiring this status.

Code of Civil Procedure section 1032 defines prevailing party to include "a defendant in whose favor a dismissal is entered, a defendant where neither plaintiff nor defendant obtains any relief, and a defendant as against those plaintiffs who do not recover any relief against that defendant. . . . [I]n situations other than as specified, the 'prevailing party' shall be as determined by the court, and under those circumstances, the court, in its discretion, may allow costs or not and, if allowed may apportion costs between the parties on the same or adverse sides. . . . " (Code Civ. Proc., § 1032, subd. (a)(4).) In conformity with this statute, the case law holds that where only one of multiple, jointly-represented defendants presenting a unified defense prevails in an action, the trial court has discretion to award or deny costs to that party. (*Webber v. Inland Empire Investments, Inc.* (1999) 74 Cal.App.4th 884, 920; *Slavin v. Fink* (1994) 25 Cal.App.4th 722, 725-726; *Smith v. Circle P Ranch Co.* (1978) 87 Cal.App.3d 267, 272.)

Plaintiff asserts the trial court did not exercise its discretion in this case, citing a statement by the trial judge during the hearing on the motion to strike AIAC's cost bill. However, the court made that comment in response to plaintiff's contention "no evidence" exists "to support any particular allocation" between AIAC and National Union, and that the latter entity presumably "fronted" AIAC's trial expenses. The record as a whole does not support a conclusion the trial court failed to exercise its discretion concerning AIAC's status and its recovery of costs.

The related arguments also fail. Contrary to plaintiff's assertion this is not a case where it established wrongdoing against AIAC, but simply failed to recover a monetary award. The jury found AIAC did not commit

fraud. Furthermore, since the injunctive relief claim had been previously dismissed, this was an action for damages. Thus, the evidence indicating AIAC subsequently modified its operating procedures concerning claims handling does not preclude it from being deemed a prevailing party.

Second, plaintiff contends the trial court erred by denying its recovery of expert witness fees under Code of Civil Procedure section 998. Nearly a year before trial, plaintiff served on National Union and AIAC an unsuccessful pretrial offer to compromise proposing "to allow judgment be taken . . . against defendants" for $626,489.26. In denying plaintiff's request for expert witness fees, the court cited *Taing v. Johnson Scaffolding Co.* (1992) 9 Cal.App.4th 579.

Code of Civil Procedure section 998, subdivision (d) authorizes the court to award a prevailing plaintiff its expert witness fees if the plaintiff made timely pretrial offer to compromise which the defendant does not accept, and "the defendant fails to obtain a more favorable judgment. . . . " In *Taing,* the court reversed an award of costs, declaring "if a plaintiff elects to submit a section 998 offer in cases involving multiple defendants, the offer to any defendant against whom the plaintiff seeks to extract penalties for nonacceptance must be sufficiently specific to permit that individual defendant to determine the exact amount plaintiff is seeking from him or her." (*Taing v. Johnson Scaffolding Co., supra,* 9 Cal.App.4th at p. 586.) *Taing* explained its rule as follows: "[A]n unapportioned offer by a single plaintiff to multiple defendants . . . requires any defendant who wants to accept to obtain the concurrence of his or her codefendants. This places a reasonable defendant at the mercy of codefendants whose refusal to settle may be unreasonable." (*Id.* at p. 585.)

National Union and AIAC were not jointly and severally liable to plaintiff. (Cf. *Steinfeld v. Foote-Goldman Proctologic Medical Group, Inc.* (1996) 50 Cal.App.4th 1542, 1547-1549.) The complaint sought recovery against National Union on theories of breach of contract, bad faith, and fraud. AIAC was alleged to be liable only on the latter theory. Furthermore, the evidence relating to each defendant's liability for fraud was separate. Thus, the trial court did not err by exercising its discretion to deny recovery of expert witness fees in this case.

NATIONAL UNION'S APPEAL

Denial of an Offset

National Union moved to have the settlement amounts plaintiff received from Ferguson and TRM offset against the damages plaintiff recovered from it. The trial court issued a lengthy written order denying the request as to both the contractual damages and the tort damages recovered by plaintiff. National Union contends the trial court erred by denying an offset in this case.

Consistent with the general rule imposing on a party the burden of proving the existence or nonexistence of each fact essential to a claim or defense (Evid.Code, § 500), "[a] defendant seeking an offset against a money judgment has the burden of proving the offset. [Citation.]" (*Conrad v. Ball Corp.* (1994) 24 Cal.App.4th 439, 444.)

With respect to plaintiff's contractual recovery, an insured is entitled to receive compensation in accordance with the policy terms, and an insurer cannot reduce the amount recoverable "merely because [the insured] has 'collateral contracts or relations with third persons which relieve him wholly or partly from the loss against which

the insurance company agreed to indemnify him.' [Citations.]" (*Strickland v. Federal Ins. Co.* (1988) 200 Cal.App.3d 792, 801, quoting *Hughes v. Potomac Ins. Co.* (1962) 199 Cal.App.2d 239, 251, disapproved on another point in *Sabella v.. Wisler* (1963) 59 Cal.2d 21, 34.) An insurer's right to recoup payment of policy benefits is covered by the principle of subrogation. To qualify for subrogation, the insurer must pay the insured's loss. (*Sapiano v. Williamsburg Nat. Ins. Co.* (1994) 28 Cal.App.4th 533, 538; *Chase v. National Indemnity Co.* (1954) 129 Cal.App.2d 853, 861- 862.)

National Union refused to pay any policy benefits to plaintiff. The cases on which it relies to establish an offset against the contract damages involve an insured's recovery of tort damages and whether the collateral source rule applied. Its contention the trial court "misread" *Kardly v. State Farm Mut. Auto. Ins. Co.* (1989) 207 Cal.App.3d 479 is incorrect. Contrary to National Union's claim, *Kardly* did not hold the insurer waives the right of subrogation by breaching the insurance contract. The part of the *Kardly* opinion National Union quotes refers to the facts of another appellate decision. (*Id.* at p. 489.) Thus, the trial court properly refused to offset the Ferguson and TRM settlements against the contractual damage award.

As for plaintiff's recovery of tort damages, the trial court agreed the collateral source doctrine did not apply because Ferguson and TRM could not be deemed collateral sources under the facts of this case. However, the court detailed the potential liability facing Ferguson and TRM, and found their potential liability exceeded $261,000 which included nonduplicative exposure exceeding $96,000. Applying the tort of another doctrine, the court concluded the settlement sums paid by Ferguson and TRM

should not be offset against plaintiff's recovery from National Union.

Generally, a party cannot obtain double recovery for the same wrong where joint or concurrent tortfeasors are jointly and severally liable for the same wrong. (6 Witkin, Summary of Cal. Law, *supra,* Torts, § 1322, at p. 779.) "[I]t has long been recognized that if one tortfeasor pays partial compensation to the plaintiff, the liability of other tortfeasors will be correspondingly reduced: '. . . payments by one tortfeasor on account of a harm for which he and another are each liable, diminish the amount of the claim against the other whether or not it was so agreed at the time of payment and whether the payment was made before or after judgment. Since the plaintiff can have but one satisfaction, evidence of such payments is admissible for the purpose of reducing pro tanto the amount of the damages he may be entitled to recover.' [Citations.]" (*Krusi v. Bear, Stearns & Co.* (1983) 144 Cal.App.3d 664, 673.)

Where tortious acts by separate persons produce the same indivisible injury, each person is liable for the whole loss even if they did not act in concert. (*Sanchez v. Bay General Hospital* (1981) 116 Cal.App.3d 776, 796.) Thus, while plaintiff sued National Union for breach of contract, breach of the implied covenant of good faith and fair dealing, and fraud, but only sought damages against Ferguson and TRM for negligence, the injury it suffered was the same.

However, the court did find the tort of another doctrine applicable to this case. "A person who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover compensation for the

reasonably necessary loss of time, attorney's fees, and other expenditures thereby suffered or incurred. [Citations.]" (*Prentice v. North Amer. Title Guar. Corp.* (1963) 59 Cal.2d 618, 620.)

Generally, a party seeking to recover litigation costs under this rule must plead and prove the claim. (*Hsu v. Abbara* (1995) 9 Cal.4th 863, 869, fn. 4.) While plaintiff did not do so here, the potential for its recovery of damages from Ferguson and TRM was made known to them during pretrial discovery. Furthermore, had it not settled with Ferguson and TRM, plaintiff could have amended the complaint to assert its right to recover the fees and expenses incurred in its action against National Union.

The record reflects National Union failed to establish the trial court erred by denying its request for an offset.

PUNITIVE DAMAGES

Introduction

Both parties attack the punitive damage award. National Union challenges the sufficiency of the evidence supporting the recovery of exemplary damages, the court's refusal to instruct the jury National Union could only be subject to punitive damages based on its own employees' conduct, and the constitutionality of the award imposed on it. Plaintiff contends the trial court erred by reducing the punitive damage award to $1.7 million.

Sufficiency of the Evidence

National Union claims its own conduct was not oppressive, fraudulent, or malicious, TRM's activity cannot be attributed to it, and it did not ratify TRM's actions.

Civil Code section 3294 authorizes the award of punitive damages in any "action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice. . . . " (Civ. Code, § 3294, subd. (a).) In *Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, the Supreme Court upheld an award of punitive damages against an insurer based on evidence two employees, a claims manager and a claims adjuster, failed to adequately investigate the insured's claims under a disability insurance policy. "The determination whether employees act in a managerial capacity, however, does not necessarily hinge on their 'level' in the corporate hierarchy. Rather, the critical inquiry is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy. When employees dispose of insureds' claims with little if any supervision, they possess sufficient discretion for the law to impute their actions concerning those claims to the corporation." (*Id.* at pp. 822-823.)

Subsequently, the Legislature amended Civil Code section 3294 to provide, "[a]n employer shall not be liable for [punitive] damages . . . based upon acts of an employee of the employer, unless the employer had advance knowledge of the unfitness of the employee and employed him or her with a conscious disregard of the rights or safety of others or authorized or ratified the wrongful conduct for which the damages are awarded or was personally guilty of oppression, fraud, or malice. With respect to a corporate employer, the advance knowledge and conscious disregard, authorization, ratification or act of oppression, fraud, or

malice must be on the part of an officer, director, or managing agent of the corporation." (Civ. Code, § 3294, subd. (b).)

In *White v. Ultramar, Inc.* (1999) 21 Cal.4th 563, the Supreme Court considered the effect of this amendment in an action for wrongful termination. The plaintiff, a convenience store employee, had been fired by a manager who was responsible for eight stores, covering sixty-five employees. The jury awarded plaintiff both compensatory and punitive damages.

In affirming, the Supreme Court concluded that "in amending section 3294, the Legislature intended (like *Egan, supra,* 24 Cal.3d at p. 823) to limit corporate punitive damage liability to those employees who exercise substantial independent authority and judgment over decisions that ultimately determine corporate policy." (*White v. Ultramar, Inc., supra,* 21 Cal.4th at p. 573.) The court noted "section 3294, subdivision (b), placed ['managing agent'] next to the terms 'officer' and 'director,' intending that a managing agent be more than a mere supervisory employee. The managing agent must be someone who exercises substantial discretionary authority over decisions that ultimately determine corporate policy. Thus, by selecting the term 'managing agent,' and placing it in the same category as 'officer' and 'director,' the Legislature intended to limit the class of employees whose exercise of discretion could result in a corporate employer's liability for punitive damages." (*Ibid.*) The critical factor "'"'. . . is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy." [Citation.]'" (*id.* at p. 573.)

The agency agreement between National Union and TRM and the evidence in this case shows TRM had broad discretion over National Union's bus insurance program. TRM could "solicit, bind, write and administer insurance" policies, and "exercise [its] independent judgment as to the time, place and manner of soliciting insurance and servicing policyholders." There was evidence AIAC directed its employees to contact TRM when seeking coverage verification. In this case, TRM participated in issuing the policy to Ko, in subsequently canceling it, and then reinstating a modified version of it. Later, when Ko submitted a claim on the bus, TRM initially issued a coverage determination, but then prepared an endorsement deleting the vehicle from the policy, and advised AIAC to deny the claim. Furthermore, TRM's president was in contact with both AIAC and the senior management of the division handling National Union's bus program when plaintiff's claim was being considered, and participated in the ultimate decision to deny it. This evidence supports the jury's conclusion TRM was National Union's managing agent, thereby subjecting it to punitive damages under Civil Code section 3294. (*White v. Ultramar, Inc., supra,* 21 Cal.4th at p. 577; *Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d at p. 823.)

In light of this conclusion it is unnecessary to consider National Union's additional claims concerning instructional error and the insufficiency of the evidence based on its own conduct.

Validity of the Trial Court's Remittitur

The trial court issued a post-judgment order conditionally granting National Union a new trial on the

insurance bad faith and fraud counts, and plaintiff's right to receive punitive damages unless the latter agreed to reduce the punitive damage award to $1.7 million. Plaintiff timely consented to the remittitur. After National Union filed its appeal, plaintiff cross-appealed and now challenges the remittitur's validity.

A trial court has the discretion to conditionally grant a new trial unless the plaintiff consents to a reduction of a damages award where the court independently determines the jury's award is excessive. (Code Civ. Proc., § 662.5, subd. (b); *Schelbauer v. Butler Manufacturing Co.* (1984) 35 Cal.3d 442, 452-453; *West v. Johnson & Johnson Products, Inc.* (1985) 174 Cal.App.3d 831, 876.) Reversal of the ruling is allowed only where there is no substantial basis in the record to support the reasons articulated by the trial court for its decision. (Code Civ. Proc., § 657; *Jahn v. Brickey* (1985) 168 Cal.App.3d 399, 408.)

The court noted the ratio of the original punitive damage award to compensatory damages (60 to 1) created a presumption the jury's verdict was the result of passion and prejudice. (*Rosener v. Sears, Roebuck & Co.* (1980) 110 Cal.App.3d 740, 752.) Plaintiff focuses much its argument on the reprehensible nature of National Union's conduct. While the court agreed the evidence supported the jury's conclusion National Union had acted reprehensibly, it concluded the jury had placed too much emphasis on National Union's financial wealth and failed to adequately consider the relationship between the injury suffered by plaintiff and the amount of the punitive damage award. The court noted this lawsuit involves an action by one corporate entity against another corporate entity to recover only for economic loss, the value of plaintiff's

security interest in a damaged bus. Given these circumstances, the trial court noted upholding the original award raised serious constitutional concerns.

Plaintiff also challenges the portion of the remittitur order requiring it to choose between a reduction in punitive damages and a new trial on *both* liability and the amount of punitive damages. In so ruling, the trial court cited *Medo v. Superior Court* (1988) 205 Cal.App.3d 64. Plaintiff relies on *Torres v. Automobile Club of So. California* (1997) 15 Cal.4th 771 in challenging the trial court's ruling.

Torres held Civil Code section 3295, subdivision (d) did not require an *appellate* court which reverses an excessive punitive damage award to order a new trial on all issues, including liability and the amount of compensatory damages. (*Id.* at pp. 777-781.) In so ruling, *Torres* distinguished *Medo*. (*Id.* at p. 780.) In *Medo,* the *trial* court ordered a new trial on all issues when the jury was discharged after completion of the liability phase. While agreeing with the plaintiffs' assertion that the defendants had waived their right to have the same jury determine both liability and the right to punitive damages, the appellate court nonetheless noted, "[p]unitive damages are not simply recoverable in the abstract. They must be tied to oppression, fraud or malice *in the conduct which gave rise to liability in the case.* Thus . . . , the instruction on punitive damages[ ] tells the jury that in arriving at an award of punitive damages, it is to consider the reprehensibility of the conduct of the defendant and that the punitive damages must bear a reasonable relation to the actual damages. In order for a jury to evaluate the oppression, fraud or malice in the conduct giving rise to liability in the case, it must consider the conduct giving rise to

liability." (*Medo v. Superior Court, supra,* 205 Cal.App.3d at p. 68.)

However, even assuming the trial court erred by relying on *Medo* to order a new trial on all issues if plaintiff refused to accept a reduction in the punitive damage award, the ruling does not require reversal. As the trial judge concluded, the jury's $10 million punitive damage award was clearly constitutionally suspect. Thus, ordering a remittitur in this case was appropriate under the circumstances.

Constitutionality of the Award

Finally, National Union contends that even the $1.7 million punitive damage award is excessive and unconstitutional. This argument lacks merit.

Punitive damages have two purposes; punish the wrongdoer and deter similar misconduct in the future by making an example of the wrongdoer. (*PPG Industries, Inc. v. Transamerica Ins. Co.* (1999) 20 Cal.4th 310, 317; *Stevens v. Owens-Corning Fiberglas Corp.* (1996) 49 Cal.App.4th 1645, 1658.) "The essential question for the jury, the trial court, and the appellate courts is whether the amount of the award substantially serves the public interest in punishment and deterrence. The California Supreme Court has established three criteria for making that determination: (1) the reprehensibility of the defendant's misdeeds; (2) the amount of compensatory damages, though there is no fixed ratio for determining whether punitive damages are reasonable in relation to actual damages; and (3) the defendant's financial condition. [Citations.]" (*Stevens v. Owens-Corning Fiberglas Corp., supra,* 49 Cal.App.4th at p. 1658.) On appeal, a judgment

awarding punitive damages is presumed to be correct and will be reversed only if the record, viewed most favorably to the judgment, reflects the award is the result of passion or prejudice. (*Ibid.*)

The United Supreme Court has recognized that an excessive punitive damage award may also violate a person's constitutional right to due process of law. (*BMW of North America, Inc. v. Gore* (1996) 517 U.S. 559, 562; *TXO Production Corp. v. Alliance Resources Corp.* (1993) 509 U.S. 443, 454.) In *BMW,* the court noted: "Elementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive fair notice not only of the conduct that will subject him to punishment, but also of the severity of the penalty that a State may impose." (*BMW of North America, Inc. v. Gore, supra,* 509 U.S. at p. 574, fn. omitted.) The court identified "[t]hree guideposts" to consider in analyzing the constitutionality of a punitive damage award: "[T]he degree of reprehensibility [of the wrongdoer's conduct]; the disparity between the harm or potential harm suffered . . . and [the] punitive damages award; and the difference between this remedy and the civil penalties authorized or imposed in comparable cases." (*Id.* at pp. 574-575.)

The record reflects the present award is permissible under both state and federal law. While it is true the loss involved only economic injury, the evidence reflects National Union engaged in reprehensible conduct. To enforce the purposes of punishing the wrongdoer and deterring similar future wrongful conduct, the award necessarily had to be large to affect a corporate entity such as National Union. "The wealthier the wrongdoer, the larger the punitive damage award must be to meet the goals of punishment and deterrence. [Citations.]" (*Stevens v.*

Owens-Corning Fiberglas Corp., supra, 49 Cal.App.4th at p. 1658.)

National Union does not dispute the fact reprehensible conduct occurred in this case. It only argues TRM, not it, committed the wrongdoing. But Civil Code section 3294, subdivision (b) permits the imposition of punitive damages on a person held vicariously liable for another's actions. National Union also focuses on the ratio between the punitive damage award and the compensatory damage award. While punitive damages must bear a reasonable relation to the actual damages suffered by the plaintiff, no fixed ratio exists to determine the proper proportion between them. (*Finney v. Lockhart* (1950) 35 Cal.2d 161, 164; *Zhadan v. Downtown L.A. Motors* (1976) 66 Cal.App.3d 481, 498.)

Thus, we conclude the award of $1.7 million in punitive damages in this case is not excessive, nor does it violate National Union's constitutional right to due process of law.

DISPOSITION

The judgment and post-judgment orders are affirmed. The motion to augment the record on appeal is granted. Each party shall bear its own costs on appeal.

RYLAARSDAM, J.

WE CONCUR:

SILLS, P.J.

O'LEARY, J.

SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF ORANGE

TEXTRON FINANCIAL CORPORATION, A Delaware Corporation, Plaintiff, vs. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA; and AMERICAN INTERNATIONAL ADJUSTMENT COMPANY, INC., Defendant.	CASE NO. 734096 ASSIGNED FOR ALL PURPOSES TO: JUDGE RAYMOND J. IKOLA DEPT. 8 ~~[PROPOSED]~~ **JUDGMENT** **TRIAL DATE: 2/26/96** (Filed May 29, 1996)

This action came on regularly for trial by jury, beginning on February 26, 1996, in Department 8 of the above-entitled Court, Honorable Raymond J. Ikola, presiding. Plaintiff Textron Financial Corporation ("Textron") appeared by its attorneys, Steven H. Gentry and David B. Ezra of Berger, Kahn, Shafton, Moss, Figler, Simon & Gladstone, and defendants National Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union") and American International Adjustment Company ("AIAC") appeared by their attorneys, R. Gaylord Smith and Michael Connally of Lewis, D'Amato, Brisbois & Bisgaard.

During the trial, the Court ruled that there was coverage for Textron's claim, as a matter of law. The Court concluded that the actions of the first named insured, Il Sung Ko, could not have terminated Textron's protection under the applicable policy.

During the trial, the Court granted National Union's motion for nonsuit, but only to the extent that Textron's complaint included allegations of a conspiracy to commit insurance bad faith. In all other respects, National Union's motions for nonsuit, and its motions for directed verdicts, were denied.

A jury of twelve persons was duly impaneled and sworn; witnesses testified; and after being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase I:

"We, the jury, find and report to the court our special verdict in phase 1 of the trial in this matter as follows:

1. What is the amount of money payable to Textron under the policy? $61,513.80.

2. Did Textron fail to mitigate its damages?

Yes ___ No __x__

3. If your answer to the previous question was yes, state the amount of damages caused by Textron's failure to mitigate: _____.

Dated: March 14, 1996

/s/
Foreperson
Jon A. Ribble"

Thereafter, the Court ruled that Textron's attorney fee damages could not exceed the law firm's contingent percentage (40%) of the amounts unreasonably withheld by National Union (together with interest).

Based on the Court's ruling, evidence of time incurred by Textron's attorneys in an effort to compel payment of policy benefits was not presented to the jury. Textron and

National Union stipulated, based on the ruling of the Court, that Textron's attorney fee recovery would be 40% of $61,513.80 (plus interest from January 25, 1994), together with expenses in the amount of $55,616.34.

After being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase II:

"We, the jury in the above entitled case, find the following on the questions submitted to us:

1. Do you find by a preponderance of the evidence that Nation[al] Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union") violated the implied covenant of good faith and fair dealing owing to Textron?

Yes x No ___

If you answer "No" to Question No. 1, then go to Question No. 5. If you answer "Yes", then answer Questions Nos. 2, 3, and 4.

2. Do you find by clear and convincing evidence that National Union was guilty of oppression in the conduct upon which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes x No ___

3. Do you find by clear and convincing evidence that National Union was guilty of malice in the conduct upon which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes x No ___

4. Do you find by clear and convincing evidence that National Union was guilty of fraud in the conduct upon which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes x No ___

5. Did either defendant make a representation as to a past or existing material fact?

National Union: Yes x No ___

AIAC: Yes x No ___

If you answer Question No. 5 "No" as to both defendants, go to Question No. 15. If you answer Question No. 5 "Yes" as to either defendant, then answer the next question.

6. Was the representation false?

National Union: Yes x No ___

AIAC: Yes x No ___

If you answer Question No. 6 "No" as to both defendants, got [sic] to Question No. 15. If you answer Question No. 6 "Yes" as to either defendant, then answer questions 7a and 7b.

7a. Did either defendant know that the representation was false when it was made?

National Union: Yes x No ___

AIAC: Yes ___ No x

7b. Did either defendant make the representation recklessly without knowing whether it was true or false?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

If you answer both Questions 7a and 7b "No" as to both defendants, go to Question No. 15. If you answer Question No. 7A or 7b "Yes" as to either defendant, then answer the next question.

8. Did either defendants make the representation with an intent to defraud the plaintiff?

National Union: Yes _x_ No ___

AIAC: Yes ___ No _x_

If you answer Question No. 8 "No" as to both defendants, go to Question No. 15. If you answer Question No. 8 "Yes" as to either defendant, then answer the next question.

9. Was the plaintiff aware of the falsity of the representation?

Yes ___ No _x_

If you answer Question No. 9 "Yes", go to Question No. 15. If you answer Question No. 9 "No", then answer the next question.

10. Did the plaintiff act in reliance upon the truth of the representation?

Yes _x_ No ___

If you answer Question No. 10 "No", go to Question No. 15. If you answer Question No. 10 "Yes", then answer the next question.

11. Was the plaintiff justified in relying upon the representation?

Yes _x_ No ___

If you answer Question No. 11 "No", go to Question No. 15. If you answer Question No. 11 "Yes", then answer the next question.

12. Did either defendant's misrepresentation cause plaintiff damage?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

If you answer Question No. 12 "No" as to both defendants, go to Question No. 15. If you answer Question No. 12 "Yes" as to either defendant, then answer the next question.

13. What is the total amount of all damage suffered by the plaintiff and caused by the reliance upon the truth of the representation?

Answer: $3859.50

If you answer Question No. 13 "No Damage", then go to Question No. 15. If you filled in a dollar amount in answer to Question No. 13, then answer the next question.

14. Do you find by clear and convincing evidence that either defendant was guilty of fraud, malice, or oppression in the conduct upon which you based your finding of liability for fraud?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

15. Did either defendant conceal or suppress a material fact?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

If you answer Question No. 15 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 15 "Yes" as to either defendant, then answer the next question.

16. Did either defendant intentionally conceal or suppress the material fact with the intent to defraud the plaintiff?

National Union: Yes _x_ No ___

AIAC: Yes ___ No _x_

If you answer Question No. 16 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 16 "Yes" as to either defendant, then answer the next question.

17. Was the plaintiff aware of the material fact at the time plaintiff acted?

Yes ___ No _x_

If you answer Question No. 17 "Yes", then sign and return the verdict. If you answer Question No. 17 "No", then answer the next question.

18. Would the plaintiff had acted in the way it did if it had known of the concealed or suppressed material fact?

Yes ___ No _x_

If you answer Question No. 18 "Yes", then sign and return the verdict. If you answer Question No. 18 "No.", then answer the next question.

19. Did either defendant's concealment or suppression of the material fact cause plaintiff damage?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

If you answer Question No. 19 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 19 "Yes", as to either defendant, then answer the next question.

20. What is the total amount of all damage suffered by the plaintiff and caused by the concealment or suppression of the material fact?

Answer: $3859.50

If you answer Question No. 20 "No Damage", then sign and return the verdict. If you filled in the dollar amount in answer to Question No. 20, then answer the next question.

21. Do you find by clear and convincing evidence that either defendant was guilty of fraud, malice, or oppression in the conduct upon which you based your finding of liability for the intentional concealment or suppression of a material fact?

National Union: Yes _x_ No ___

AIAC: Yes _x_ No ___

Please sign and date this verdict form.

Jon A. Ribble
Dated: April 11, 1996 /s/
Foreperson

Based upon this verdict, the Court determined that AIAC was entitled to judgment in its favor.

After being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase III:

"We, the jury in the above entitled action, find the following special verdict on the questions submitted to us:

1. Shall punitive damages be assessed against defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania?

Yes x No ___

If your answer is "yes," please answer the next question. If your answer is "no," have your foreperson sign and date this special verdict.

2. We assess punitive damages against National Union Fire Insurance Company of Pittsburgh, Pennsylvania, as follows:

$10,000,000.00

Please sign and date this verdict form.

Jon A. Ribble
Dated: April 12, 1996 /s/
Foreperson

NOW, THEREFORE, IT IS ADJUDGED, ORDERED, AND DECREED as follows:

Plaintiff Textron Financial Corporation shall have and recover judgment against defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania:

1. For general and compensatory damages, $165,414.40 (representing $61,513.80 in unpaid policy benefits, $14,156.60 in interest on unpaid benefits from January 24, 1994 to May 14, 1996, $85,884.50 pursuant to *Brandt v. Superior Court*, and $3,859.50 in additional damages on the fraud cause of action);

2. For punitive damages, ten million dollars ($10,000,000.00);

3. Plus costs and disbursements in the amount of $39,280.31*. [10/8/96 MIS] [*(Per order of 7-29-96)]

Defendant American International Adjustment Company shall have judgment against plaintiff Textron Financial Corporation and shall recover costs and disbursements in the amount of $10,277.52 [(Per m o of 10-3-96)]

DATED: 5/29/96 By: Raymond J. Ikola
RAYMOND J. IKOLA,
Judge of the Superior Court

SUPERIOR COURT OF THE
STATE OF CALIFORNIA
COUNTY OF ORANGE

TEXTRON FINANCIAL CORPORATION, a Delaware corporation, Plaintiff, vs. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al., Defendants.	CASE NO. 73 40 96 RULING AND ORDER CONDITIONALLY GRANTING NATIONAL UNION'S MOTION FOR NEW TRIAL (Filed Jul. 29, 1996)

The court, having read and considered the Motion for New Trial filed herein by defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union"), together with the papers filed in opposition to the motion by plaintiff Textron Financial Corporation ("Textron") and the papers filed in reply to the opposition by National Union, and having heard and considered the arguments made by both parties at the hearing on the motion on July 25, 1996, now rules as follows:

National Union's Motion for New Trial is granted as to the causes of action for fraud and for breach of the implied covenant of good faith and fair dealing and the award of punitive damages on the ground that the award of punitive damages is excessive. The new trial will be as to National Union only. Provided, however, that the order granting a new trial is denied if Textron consents to a reduction of the $10 million award of

punitive damages in the amount of $8.3 million to a total award of punitive damages in the amount of $1.7 million ($1,700,000.00). The court, in its independent judgment, has determined from the evidence that a punitive damage award of $1.7 million is fair and reasonable.

The reasons the court has conditionally granted the motion for new trial on the ground of excessive damages are as follows.

The jury was instructed, in connection with making its determination of whether to award punitive damages, to consider: (i) the reprehensibility of the conduct of the defendant; (ii) the amount of punitive damages which will have a deterrent effect on the defendant in the light of defendant's financial condition; and (iii) that punitive damages must bear a reasonable relation to the injury, harm, or damage actually suffered by the plaintiff." BAJI 14.72.2 The court has concluded that the jury gave undue emphasis to the second factor, i.e., the amount of damages which will have a deterrent effect in light of the defendant's financial condition, and insufficient emphasis to the third factor, i.e., the relationship between the damage suffered and the amount of the award. The punitive damages awarded by the jury amounted to slightly more 60 times the total compensatory award. In *Rosener v Sears, Roebuck & Co.*, 110 Cal.App.3d 740, 752 (1980), the court referred to an award in which the ratio of punitive to compensatory damages was approximately 63 to 1, with a difference in the awards of $9.85 million, as "grossly disproportionate," raising "a presumption that it was the result of passion or prejudice." *Id.* at 752. In the case at bar the ratio of punitive to compensatory damages is 60 to 1,

and the difference is $9.83 million. The same presumption of passion or prejudice is as apparent in this case as it was in *Rosener*. The amount awarded by the jury greatly exceeds that which is necessary to deter future conduct of the type shown by the evidence in this case.

Further, the court is obliged to examine the award in light of the federal due process "guideposts" outlined by the U.S. Supreme Court in *BMW of North America v Gore*, 96 D.A.R. 5747 (May 20, 1996), a decision announced after the jury reached its verdict. The first guidepost, described by the *BMW* court as "perhaps the most important indicium of the reasonableness of a punitive damages award" is "the degree of reprehensibility of the defendant's conduct." This guidepost matches one of the factors given to the jury to consider in this case consistent with *Neal v Farmers Ins. Exchange*, 21 Cal.3d 910, 928 (1978). Although the court finds that the jury had sufficient evidence to find that National Union's conduct was sufficiently reprehensible to merit the imposition of punitive damages, the court also notes, as did the Supreme Court in *BMW*, that the harm inflicted was purely economic in nature. Nothing done by the defendant showed any "indifference to or reckless disregard for the health or safety of others." *BMW* at 5750. This factor has also been used by California courts in the process of assessing the reprehensibility of the defendant's conduct when reviewing a punitive damage award. For example, the court in *Seeley v Seymour*, 190 Cal.App.3d 844, 867 (1987) observed that the parties in that case were sophisticated businessmen of relatively equal bargaining strength, and thus the situation carried "a lesser degree of 'reprehensibility'" than the more typical punitive damage case where a large or

sophisticated business enterprise uses its wealth or power to exploit the weak or the unwary. *Id.* The court concludes that in this case as well, the parties were both large business enterprises, neither of which was able to exploit the other.

The second *BMW* guidepost is the ratio of the punitive damages to the actual harm. This factor has been addressed above under California law. The U.S. Supreme court has stated that it is impossible to "draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable that would fit every case." The Court reiterated, however, that a "general concern of reasonableness properly enters into the constitutional calculus." As noted above, this court concludes that a ratio of 60 to 1 raises a presumption of jury passion or prejudice. Consistent with a "general concern of reasonableness," the court also concludes that permitting this award to stand would make it constitutionally suspect.

The third *BMW* guidepost is a consideration of sanctions adopted by the legislature for comparable misconduct. National Union points to Insurance Code 790.035(a) which imposes a penalty of up to $10,000 for each act in violation of section 790.03. While this court has concluded that the punitive damage award is excessive for the other reasons stated above, the utilization of section 790.035(a) as a guidepost is of significantly less importance. It is noted that the "guideposts" reviewed by the Supreme Court were all for the purpose of assisting the court in determining whether the defendant received "fair notice not only of the conduct that will subject [it] to punishment but also of the severity of the penalty that a State may impose." *BMW* at 5750. Despite the civil

penalties provided by Section 790.035, California has a long history of permitting punitive damage awards where the evidence is sufficient to establish fraud or the malicious or oppressive breach of the covenant of good faith and fair dealing. Surely National Union does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law. It is also significant to observe in this connection that despite the long history of these awards under the common law, the California legislature has not acted to impose any statutory limitation on such awards as it has, for example, with respect to negligence actions against health providers.

Accordingly, as noted at the outset, the court concludes that the punitive damage award in this case is excessive. Because the same jury must determine both punitive damages and liability, *Medo v Superior Court*, 205 Cal.App.3rd 64, 66-68 (1988), a new trial is ordered on the causes of action for fraud, breach of the covenant of good faith and fair dealing, and on the award of punitive damages. The new trial will be as to National Union only. The court has determined from the evidence, however, that an award of $1.7 million for punitive damages would be fair and reasonable. Therefore, if plaintiff files its written consent to reduce the award of punitive damages to the amount of $1.7 million, the motion for new trial will be denied. CCP 662.5. Plaintiff's written consent to the remittitur, should it choose to do so, is to be filed and served within 15 days of the date of this order.

Clerk to give notice to the parties

Dated: July 29, 1996 /s/ Raymond J. Ikola
Raymond J. Ikola
Judge of the Superior Court

Court of Appeal, First Appellate District, Division Four – No. G020323

S095924

IN THE SUPREME COURT OF CALIFORNIA

En Banc

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al,
Defendants and Appellants.

(Filed May 2, 2001)

Petition for review DENIED.

GEORGE
Chief Justice

Court of Appeal, Fourth Appellate District,
Division Three – No. G020323

S095924

IN THE SUPREME COURT OF CALIFORNIA

En Banc

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al,
Defendants and Appellants.

(Filed May 4, 2001)

The order filed on May 2, 2001, is hereby modified to reflect the above-captioned corrected district and division.

/s/ George
Chief Justice

Court of Appeal, Fourth Appellate District,
Division Three – No. G020323

S108979

IN THE SUPREME COURT OF CALIFORNIA

En Banc

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al,
Defendants and Appellants.

(Filed Sep. 25, 2002)

Petition for review DENIED.

GEORGE
Chief Justice

Supreme Court U.S.
FILED
JAN 27 2003
OFFICE OF THE CLERK

No. 02-966

In The
Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

v.

TEXTRON FINANCIAL CORPORATION,

Respondent.

On Petition For Writ Of Certiorari To The California Court Of Appeal, Fourth Appellate District

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Does the United States Constitution limit punitive damages by imposing a mathematical formula that calculates a specific ratio of punitive to compensatory damages?

2. Does an appellate court reviewing a punitive damages award commit constitutional error when it looks to factors in addition to comparable civil and criminal penalties in determining whether an insurance company had adequate notice that its fraudulent claims handling conduct could warrant substantial punitive damages?

TEXTRON'S RULE 29.6 STATEMENT

Textron Financial Corporation is a wholly-owned subsidiary of Textron, Inc.

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INTRODUCTION

This case involves an insurance company (National Union) that fabricated policy documents after an accident to fraudulently and retroactively negate insurance coverage.

A jury assessed $10 million in punitive damages against National Union. But the trial judge reduced the punitive damages by 83%. Despite the egregious nature of the wrongdoing, and despite the trial judge's substantial reduction of punitive damages, National Union continues to challenge the result even though it has already been through the appellate process twice.[1]

The reduced $1.7 million award was well within constitutional limits. Even National Union acknowledges that the involved conduct was extreme and outrageous. After it found out about the accident, the insurance company fabricated documents to make it appear as if insurance coverage had been eliminated before the accident. This was affirmative and outright fraud. As the fraud started to surface, concealment efforts were undertaken. Documents were removed from files and destroyed. Important information was obscured. Even during the trial, National Union simply destroyed documents to keep them from the jury.

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[1] This was one of several cases in which this Court granted certiorari, vacated the judgment, and remanded in light of *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001). See *National Union Fire Ins. Co. v. Textron Financial Corp.*, 534 U.S. ___, 122 S.Ct. 340 (2001). On remand, the California Court of Appeal again affirmed the judgment and the California Supreme Court again denied review.

The ratio of punitive to compensatory damages was 10:1. But when the harm and potential harm that resulted from National Union's fraudulent conduct are considered, the ratio dropped to 3:1 or less. The civil and criminal penalties that attach to similar misconduct are substantial. Insurance fraud is punishable by up to five years imprisonment plus hefty fines. On the civil side, the California Department of Insurance can punish such conduct by assessing fines of up to $55,000 and, if necessary, by terminating an insurance company's license to sell insurance in California.

Even if there was room to reasonably debate whether the jury's original $10 million verdict was within constitutional limits, there was no doubt that the judicially-reduced $1.7 million punitive damages judgment was well within constitutional limits.

During the seven years this case has been on appeal, National Union's arguments have always varied and often conflicted. And if the actual facts were anything close to those National Union describes, the jury would have found in favor of National Union, not against it.

In its latest attack on a judgment that has already withstood extensive appellate review, National Union argues that the United States Constitution mandates a rigid mathematical rule placing an absolute maximum limit on a state's ability to impose punitive damages, even in situations where overt fraudulent misconduct was committed by an insurer that was required under state law to treat its policyholders with utmost good faith and fair dealing. Textron does not believe that the Constitution includes such a rigid mathematical formula. But even if it did, it would have no impact on this case. Using a correct

assessment of compensatory damages, the punitive award as reduced by the court was only a 10:1 ratio. And when the actual harm and potential harm is considered, the ratio drops to 3:1 or less.

National Union's petition should be denied. This is *not* a case where National Union was punished for out-of-state conduct. This is *not* a case involving conduct that was perfectly legal in other states. This is *not* a case where a jury assessed hundreds of millions dollars in punitive damages. This isn't even a case where the jury's verdict was allowed to stand. To the contrary, this is a case where National Union was very fortunate to have a trial judge dramatically reduce the jury's verdict even though National Union was caught engaging in post-accident policy manipulation, and even though National Union staunchly ratified and defended the wrongdoing all the way through trial. There is no issue worthy of further review by this Court.

FACTUAL BACKGROUND

This trial lasted more than a month and a half, and generated a record that exceeded 10,000 pages. Textron's task of presenting the facts is made more difficult because National Union's petition (like its prior petition in 2001) recites an incomplete and inaccurate version of events.

In early 1992, Textron loaned Il Sung Ko $87,000 to buy a tour bus for his business. To protect itself, Textron had Ko obtain insurance covering Textron's security

interest in the bus. Ko bought insurance from National Union. Textron was named as an additional insured under the policy. PA 3a.[2]

After the 1992 Los Angeles riots, Ko faced a slowing tourism business and cash flow problems. Douglas Ferguson, Ko's broker, advanced a premium payment for Ko. Nevertheless, on October 22, 1992, National Union sent Ko a cancellation notice which said the policy would cancel as of November 27, 1992. PA 4a.

Aware that Ko was not using some of the six buses in his fleet, Ferguson wrote to TRM International, Inc., National Union's managing general agent for bus insurance, and asked if a new policy could be issued "with only four units." In response to Ferguson's inquiry, George Peare, a TRM underwriter, responded by suggesting a lay-up credit, a "much easier way of doing it." According to Ferguson, discussion about the lay-up credit was limited. He was told to "Get the license plates. Get the license plates." App. 3.

Lay-up credits are a form of mileage rating. The risk of loss is reduced where fewer total miles are being driven. So an insurer that offers a lay-up credit reduces the premium when vehicles are not in regular use. Unlike deletions, lay-up credits do not eliminate or even reduce coverage. Because full coverage remains in effect, insurance companies that issue lay-up credits typically ask for

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[2] Citations to petitioner's appendix are referenced as "PA." Citations to respondent's appendix, which consists primarily of an excerpt from a brief below containing record references, are abbreviated "App."

license plates to minimize the likelihood that a laid-up vehicle will be used on a daily basis. App. 3.[3]

This lay-up credit was advantageous for National Union since it kept the policy in force, allowed National Union to continue collecting monthly premium payments of about $5,000, required very little paperwork, and did not require notice to other parties. App. 3.

A few days after the policy was cancelled for non-payment of premium (without notice to Textron), Ko made a partial premium payment and sent the license plates for two of his six buses to Ferguson. By December 2, 1992, National Union had implemented the lay-up credit, and the policy was reinstated in full, with no reduction in coverage. App. 3-4.

Ko's broker, Ferguson, did not understand the difference between lay-up credits and deletions. Ferguson thought lay-up credits and deletions were the same thing. He incorrectly assumed that lay-up credits and suspensions terminated coverage. App. 4.

Ferguson also wanted to make sure he recovered the premium he had advanced. So after National Union reinstated the policy, Ferguson continued to send notes to TRM which emphasized that he had the license plates. App. 4. However, since the lay-up credit had already been

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[3] "Deletions," on the other hand, eliminate coverage for the deleted vehicle. Deletions typically occur when a policyholder sells a vehicle to a third-party. If insurance companies made policyholders turn in license plates when coverage was deleted, policyholders would not be able to sell their vehicles. As a result, policyholders are not required to turn in license plates when the insurer deletes a vehicle from coverage.

issued, and the policy fully reinstated, TRM did not bother to respond.

Then, January 7, 1993, one of Ko's buses broke down. The Textron-financed bus was sent to pick up stranded passengers, and it was severely damaged when it hit a patch of ice and slammed into a truck. Since Ferguson erroneously believed lay-up credits eliminated coverage, he told Ko the accident was not covered. However, Ferguson presented a claim to National Union. PA 4a-5a.

Because the lay-up credit had resulted in a full policy reinstatement, TRM – the underwriting company that handled administration of bus insurance policies for National Union – verified coverage on February 4, 1993. App. 4-5. But a claims adjuster subsequently spoke to Ko's assistant (neither Ko nor his assistant spoke English as a first language). The adjuster quickly learned that Ko had erroneously been told that there was no coverage for the accident. National Union's adjuster decided not to tell Ko that coverage had already been verified, explaining that "coverage is usually, in my experience, only discussed with an insured if it's a problem." App. 5.

At least one claims adjuster wanted to review the actual policy before denying the claim. Claims adjusters had been instructed to contact John Lavin (an underwriting manager in National Union's Home Office) "for a complete policy copy." The claims office did request a copy of the policy, but National Union's Home Office refused to release the policy, even to its own adjusters. App. 5.

Because National Union's Home Office refused to allow access to the actual policy, claims personnel turned to the TRM claims supervisor, Dick Longuil. But Longuil worked in New York, eight hours away from TRM's New

Jersey office. As a result, Longuil did not have access to any file materials. App. 5.

Even without documents, however, Longuil immediately had "a bad feeling about" the accident. Among other things, he was troubled by the possibility of personal injury claims that could become very costly for National Union. App. 5-6.

A few days later, even though TRM had previously verified coverage, National Union denied Ko's claim (and the claim that had been presented for the owner of the truck the bus had hit). National Union said coverage had been cancelled before the accident. The claims were denied even though TRM had verified coverage; even though the policy had been fully reinstated before the accident; and even though the insurance policy National Union maintained at its Home Office included a lay-up credit endorsement, and no deletion endorsement. PA 5a-6a.

As of February 1993, no one had told Textron about the policy cancellation, the lay-up credit, the policy reinstatement, the accident, or the coverage verification. App. 6.

Ko continued making loan payments as long as he could. But by late 1993, he defaulted on his Textron loan. Textron then learned that the bus had been involved in an accident earlier that year. When it inquired, Textron was falsely told that coverage was terminated before the accident. As a result, Textron was required to sue Ko. But without insurance for the loss, Ko was soon forced into bankruptcy. PA 5a.

National Union formally denied Textron's claim based on the false contention that National Union couldn't tell

Textron about the coverage termination because National Union itself did not have advance notice of the cancellation. National Union's denial letter did not disclose the lay-up credit, the reinstatement, or the fact that coverage had been verified after the accident. App. 6.

Textron had started asking for a copy of the National Union insurance policy in January 1994. Two months later, in March 1994, National Union finally gave its own claims adjusters a copy of the original Home Office policy. But National Union decided to withhold the policy from Textron. App. 6.

Rather than give Textron a copy of the original policy, National Union waited another five months and then it gave Textron a different version of the policy. This new version of the policy conveniently replaced the credit endorsement with a falsified "deletion" endorsement – a falsified document that had been created long after the accident. PA 5. No witness who testified at trial could offer any legitimate reason why National Union would withhold the original Home Office policy from Textron. App. 7. The jury had no choice but to conclude that National Union's Home Office was trying to conceal the fraud by keeping that version of the policy away from Textron.

Textron sued National Union in August 1994. National Union adopted an unusual litigation strategy. It embraced and endorsed everything TRM did (except when TRM verified coverage). Instead of arguing that TRM had defrauded everyone, National Union accused Textron of trying to "set up" the claim. While blaming Textron, National Union praised TRM, telling the jury "TRM did what it did openly, candidly, without trying to fool anybody."

National Union was so antagonistic toward Textron that even after TRM officially acknowledged that a lay-up credit issued following a request for license plates would not terminate coverage, National Union continued to attack Textron and continued to deny Textron's claim for insurance benefits.

By the end of the trial, everyone in the courtroom knew National Union had been caught perpetrating a serious fraud. National Union had issued a lay-up credit and fully reinstated the policy *before* the accident. There never was any pre-accident "deletion." But because it was worried about possible personal injury claims that might have come from passengers on a seriously damaged tour bus, and because it knew Ko could barely speak English and his broker did not know about lay-up credits, National Union had fabricated and concealed documents to fraudulently and retroactively terminate coverage.

From start to finish National Union tried to conceal evidence and deceive Textron and others. When it started responding to Textron's claim, National Union chose not to mention important facts, such as the fact that the policy had been fully reinstated before the accident. App. 8. To prevent Textron from learning that the fabricated deletion endorsement had been created after the accident, a "certificate of mailing" was placed over the purported creation date before the falsified "deletion" version of endorsement No. 8 was faxed to Textron. App. 8-9.[4]

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[4] The "certificate of mailing" offered further evidence of deception. For example, there was no corresponding "certificate of mailing" for the other bus that was supposedly "deleted." If National Union had been

(Continued on following page)

Similarly, National Union's Home Office withheld the original policy, because even as of October of 1993 (nine months after the accident), there was still no "deletion" endorsement in the actual policy – only a credit endorsement. App. 7.

During trial, the jury also learned that National Union's underwriting file had been manipulated before it was produced to Textron. The file manipulation was exposed because Ferguson's file included lay-up credit-related correspondence that had been removed from the underwriting file. For example, Exhibit 15 was the underwriter's "much easier way of doing it" letter. The "much easier way of doing it" obviously referred to a lay-up credit. But Exhibit 15 (and other similar documents) had been removed from the underwriting file before the file was produced to Textron. App. 9-10.

Even in mid-trial, National Union destroyed documents to keep them from the jury. For example, National Union's Portland claim file was housed in a jacket that would have reflected important claims information. Nevertheless, National Union produced only part of the file, explaining that "some idiot" had destroyed the file's jacket before it could be made available to Textron. There was no legitimate reason to destroy the jacket. In fact, without the jacket, there was nothing to hold the file together. App. 10.

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providing routine "deletion" notices, it would have prepared "certificates of mailing" for both buses, not just the bus that had been involved in an accident. App. 9.

The evidence permitted only one reasonable conclusion – that National Union had perpetrated a serious fraud and then tried to cover it up. In fact, the conduct was so egregious that even National Union's own attorney conceded during closing arguments that unless the jury believed National Union's witnesses, this conduct was "vile."

In addition to insurance bad faith, the jury determined that National Union committed fraud through both affirmative misrepresentation and concealment. Applying California's heightened clear and convincing evidentiary standard, the jury also found that National Union acted with malice, with fraud *and* with oppression.

POST-TRIAL PROCEDURAL HISTORY

Following trial and entry of judgment, National Union moved for a new trial and asked the trial judge to reduce the jury's verdict based on *BMW of North America v. Gore*, 517 U.S. 559 (1996).

Ironically, the trial judge acknowledged the obvious reprehensibility of the misconduct, but reduced the jury's punitive damages verdict from $10 million to $1.7 million despite observing that:

> Surely National Union does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law.

PA 76a.

When it appealed the ruling, National Union made a wide array of sometimes contradictory arguments. National Union started with a laundry list of arguments centered squarely on state law issues – such as jury instructions pertaining to the state law definition of a "managing agent," common law principles of "offset" and ratification, and various state law standards for tort liability.

In its unpublished opinion, the Court of Appeal affirmed, disposing of a wide array of issues National Union had raised. The California Supreme Court denied National Union's petition for review. PA 78a-79a.

National Union then petitioned this Court, questioning the standard of review the California Court of Appeal had applied. Without issuing any opinion, this Court vacated the judgment and returned it to the California Court of Appeal for further evaluation in light of *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001). See *National Union Fire Ins. Co. v. Textron Financial Corp.*, 534 U.S. ___, 122 S.Ct. 340 (2001).

The California appellate court's second review of this case unequivocally applied a "de novo" standard of review. The court again decided that the $1.7 million punitive damages judgment was constitutional even if the jury's original $10 million verdict was questionable. PA 27a-32a. Having obtained its undeniably independent review, National Union was still unsatisfied. It again petitioned the California Supreme Court for further review. National Union argued that the court of appeal had "failed to conduct a de novo review." And it argued that even the substantially reduced $1.7 million punitive damages judgment was excessive because National Union could not have had fair notice of the fact that the post-accident

fraudulent manipulation of the insurance policy could result in a punitive damages award approaching $2 million. Predictably, the California Supreme Court denied National Union's petition for review. PA 80a.

Now, having already forced Textron to incur legal fees and expenses that approximate the $1.7 million punitive damages assessment, National Union files yet another certiorari petition.

REASONS WHY NATIONAL UNION'S PETITION SHOULD BE DENIED

National Union does not argue that this case satisfies the traditional and accepted standards for invoking this Court's discretionary review. Indeed, this was an unpublished appellate court decision followed by a summary denial of review in the state's supreme court.

Having run out of arguments, National Union now suggests that the Constitution includes a rigid mathematical formula that is mechanically applied to constrain all punitive damages awards. This is not and should not be the law, so there is nothing to "clarify" and no need for "guidance." See petn. at 12, 16.

1. THE DUE PROCESS CLAUSE CANNOT BE REDUCED TO A SIMPLE MATHEMATICAL FORMULA

Having failed to convince any court that there was any constitutional problem with the $1.7 million punitive damages judgment in a case where the insurance company was caught changing an insurance policy after an accident in order to try to avoid a series of accident-related claims,

National Union now argues that the Constitution should be interpreted to impose a rigid mathematical formula that limits all punitive damages assessments.

There are at least two basic problems with National Union's argument. First, the Constitution does not include a rigid mathematical formula that mechanically caps all punitive damages awards. Second, even if the Constitution included such a mathematical formula, it would not be operative in this case. To try to make the ratios look bigger than they really are, National Union has misstated California law. And National Union has ignored the harm and potential harm courts consider when evaluating punitive damages awards.

A. The Constitution Does Not Impose a Rigid Mathematical Formula

As this Court reiterated in *BMW of North America, Inc. v. Gore*, 517 U.S. 559, 582 (1996), "we have consistently rejected the notion that the constitutional line is marked by a simple mathematical formula, even one that compares actual *and potential* damages to the punitive award." (Original emphasis.)

One court explained the problem with the rigid mathematical formula National Union advocates as follows:

> A mechanical ratio, such as two to one or three to one or four to one or even ten to one, would not make good sense. The smaller the compensatory damages, the higher the ratio of punitive to compensatory damages has to be in order to fulfill the objectives of awarding punitive damages.

Cooper v. Casey, 97 F.3d 914, 919 (7th Cir. 1996).

As a result, the ratio between the harm or potential harm caused by a defendant and the punitive damages is only one of several factors a court considers when assessing the question of whether a defendant had "fair notice . . . of the severity of the penalties that a state may impose." *BMW*, 517 U.S. at 574.

B. National Union Has Inaccurately Calculated the Applicable Ratio

Although the figure is never mentioned in National Union's petition, Textron's actual compensatory damage award was $165,414.40. PA 2a. The punitive damages part of the judgment was $1.7 million – a ratio of 10:1, *not* 20:1.

National Union seems to suggest that half of the compensatory damages should be ignored because they consist of insurance policy benefits National Union wrongfully withheld by concealing the lay-up credit that resulted in a pre-accident reinstatement of the policy. National Union says policy benefits that are wrongfully withheld are purely contractual and cannot be recovered in tort. Even if that was true (and it is not), it would not change the fact that the ratio of punitive to compensatory damages was only 10:1, not 20:1.

There are, however, other problems with the mathematical formula that serves as the basis for National Union's petition. For example, National Union's self-serving approach ignores the fact that the wrongful withholding of policy benefits causes harm. In addition, under California law, insurance policy benefits that are wrongfully withheld *are* recoverable in tort. As one court explained, "the violation of [the duty of good faith and fair dealing] sounds in tort notwithstanding that it may also

constitute a breach of contract." *Fletcher v. Western National Life Ins. Co.*, 10 Cal.App.3d 376, 401 [89 Cal.Rptr. 78, 93] (1970).

The California Supreme Court reached the same conclusion a few years later, noting that breach of "the duty of an insurer to deal fairly and in good faith . . . sounds in both contract and tort. . . . " *Gruenberg v. Aetna Ins. Co.*, 9 Cal.3d 566, 573 [108 Cal.Rptr. 480, 484] [510 P.2d 1032, 1036] (1973).

In *Brandt v. Superior Court*, 37 Cal.3d 813, 817 [210 Cal.Rptr. 211, 213] [693 P.2d 796, 798] (1985), the California Supreme Court again held that when an insurer unreasonably withholds policy benefits, the policyholder has a "cause of action in tort" and the insurance company is "liable for any damages which are the proximate result of that breach."

National Union refused to pay the policy benefits that were due and owing to Textron even though TRM had verified coverage after the loss. The jury found that National Union committed the tort of bad faith when it withheld those policy benefits. In addition, the jury found that National Union committed fraud through various concealments and overt misrepresentations. National Union was liable not just for insurance bad faith (which is itself a tort in California), but also for outright fraud. Altogether, the compensatory damages were $165,414.40. Even when the ratio is limited to a consideration of the actual compensatory damages award, the ratio is only 10:1, *not* 20:1.

As National Union has reluctantly acknowledged, ratios substantially in excess of 10:1 are routinely upheld in situations where defendants have been caught trying to

use fraud and deceit to make money. For example, in *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443 (1993), this Court upheld a $10 million punitive damages award against compensatory damages of only $19,000 – a ratio of over 500:1.

C. National Union Forgets to Evaluate the Harm and Potential Harm That Arose From Its Conduct

In assessing ratios, this Court has noted that a strict assessment of actual compensatory damages is not required. Instead, courts consider the potential harm that could have resulted because of the defendant's conduct. *TXO*, 509 U.S. at 460. When the full panoply of harm and potential harm is considered, the ratio in this case drops from 10:1 to 3:1 or even less. For example, even though Textron's attorneys spent over 1,500 hours trying to get National Union to honor the claim, the trial court capped the legal fee component of Textron's damages at just over $30,000. If the trial court had allowed the jury to award damages based on a reasonable hourly rate (or if Textron had initially hired its attorneys on an hourly basis), the compensatory damages award would have approached or exceeded $500,000.

In addition, National Union's conduct placed Ko in bankruptcy, destroying the business relationship between Ko and Textron. And even though TRM advised National Union that it was "stuck for liability," National Union denied the third-party liability claim that was presented by the insurer for the truck the Textron-financed bus hit.

Finally, National Union concealed the lay-up credit and pre-accident reinstatement of the policy at least in

part because TRM and National Union were worried about possible passenger personal injury claims. As it turns out, the bus accident occurred while the bus was on the way to pick up passengers who had been stranded when another bus broke down, not when it was loaded with passengers. But before the fraud was implemented, TRM had advised that it was "really concerned about this accident," and "would not be surprised" by personal injury claims. As late as September 1994, National Union's Home Office was still concerned about the "potential B[odily] I[njury] claims." Fearing that the bus was loaded with passengers at the time of the accident, National Union was counting on its fraudulent conduct to help save hundreds of thousands of dollars, at the very least. So when the actual harm and potential harm is considered, the ratio drops to something approaching 1:1.

D. Other Facts Also Supported the Constitutionality of the Punitive Damages Assessment

Even National Union admits that *BMW* identified various circumstances in which very high ratios between punitive and compensatory damages may be particularly appropriate. For example, when the compensatory damages are relatively low, a higher ratio may be necessary to fulfill the function of punitive damages. Likewise, in situations where the harm is hard to precisely value, a higher ratio may be necessary to fulfill the function of punitive damages. *BMW*, 517 U.S. at 582.

Although the ultimate ratio was not high, this case involved all of the factors *BMW* identified. The compensatory award was relatively low, particularly considering that Textron was a substantial corporation and National

Union had a net worth of over $3.5 billion at the time of trial. During the trial, National Union's attorney repeatedly referred to the claim as "small" or "little." And at least one National Union underwriting official tried to convince the jury that he decided not to get very involved in the claim precisely because it was so small.

In addition, the conduct was particularly egregious. Affirmative fraud and deceit is bad enough when committed by anyone. But when the company that commits the fraud is charged with a strict duty of utmost good faith and fair dealing under state law, the reprehensibility of the wrongdoing is magnified.[5]

The harm National Union caused also had elements that were hard to value. For example, there is no easy way to place a value on the harm that was done when National Union forced Ko into bankruptcy and destroyed the business relationship between Textron and Ko.

Properly considered, the ratio between the punitive damages and harm suggested that the jury's $10 million

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[5] This Court has held that "the federal excessiveness inquiry appropriately begins with an identification of the state interest that a punitive award is designed to serve." *BMW*, 517 U.S. at 568. California has a compelling state interest in deterring state-licensed insurers from engaging in fraud as a means of unfairly and improperly denying insurance claims. The California Supreme Court has repeatedly acknowledged California's strong interest in promoting fair handling of insurance claims. *See, e.g., Egan v. Mutual of Omaha Ins. Co.*, 24 Cal.3d 809, 819-820 [620 P.2d 141, 145-146] [169 Cal.Rptr. 691, 695-696] (1979). California state law actually requires policyholders to report punitive damage awards against insurers to a state agency in order to help the state police insurers who engage in malicious conduct toward policyholders. Cal. Civ. Code § 3296.

verdict was within constitutional limits. But even if there was room to debate the validity of the jury's $10 million verdict, the reduced $1.7 million judgment fits well within constitutional limits.

2. THE CALIFORNIA COURT OF APPEAL PROPERLY APPLIED THE THIRD *BMW* GUIDEPOST

National Union also argues that the California Court of Appeal misapplied the third *BMW* guidepost – criminal or civil penalties that might be assessed for similar misconduct.

National Union starts by trying to divorce the guidepost from its ultimate function. The reason other criminal and civil penalties are considered is to evaluate whether the defendant had adequate notice that misconduct of the type proved at trial could result in a multi-million dollar punitive damages assessment. *BMW*, 517 U.S. at 574. Then National Union compounds its error by arguing that there is no misconduct to evaluate. As National Union tells the story, only TRM did anything wrong. And although TRM was National Union's managing general agent, and although the acts of a managing general agent are considered to be those of the insurer itself under California law, National Union simply declares that it is blameless and cannot be evaluated under the third *BMW* guidepost.[6]

The assumption underlying National Union's argument that "it can't be punished because it didn't do anything

[6] Under California law, "the acts of the [managing general agent] are considered to be the acts of the insurer on whose behalf it is acting." Cal. Ins. Code § 769.85.

wrong" is inaccurate and invalid. It is well settled that punitive damages can be assessed against an insurance company because of the actions of its agents or managing agents. So even if National Union had never become directly involved in denying the claim or manipulating the policy, and even if it had not repeatedly ratified all of the wrongful conduct, National Union would still be subject to punitive damages.

For example, this Court upheld a significant punitive damages award in a case involving an insurance sales agent's conduct. *Pacific Mutual Life Ins. Co. v. Haslip*, 499 U.S. 1 (1991) (approving punitive damages award equal to 200 times out-of-pocket expenses based on an insurance company's sales representative's conduct).[7]

In addition, the California Court of Appeal did *not* decide that TRM was the only wrongdoer. In fact, all the way through trial, National Union stubbornly defended TRM's conduct. Far from blaming TRM, National Union boldly told the jury that the important decisions were actually made by National Union's "senior brass out of New York, who were familiar with the underwriting of this

[7] In California, punitive damages can be assessed based on the conduct of "managing agents." In other jurisdictions, punitive damages can be assessed against corporations based on the conduct of agents, even if those agents are not managing agents. *See, e.g., Davis v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 906 F.2d 1206, 1221-22 (8th Cir. 1990) (approving a $2 million punitive damages award against compensatory damages of $100,000 based on conduct of a corporate agent).

claim. . . . Senior underwriters in New York who know this stuff inside and out. . . . "[8]

National Union changed its strategy on appeal. For the first time, National Union's appellate briefing started to suggest that TRM had actually committed the wrongdoing, and that National Union did not really know what TRM was doing. This, of course, was factually preposterous. It was National Union that decided to deny the claim even though TRM verified coverage after the accident. It was National Union that misrepresented the terms of the policy in the denial letter. It was National Union, not TRM, who withheld the Home Office policy that had a credit endorsement, rather than a deletion endorsement. It was a National Union underwriter, not a TRM employee, who testified that license plates are requested when lay-up credits are issued, but not when coverages are deleted. And even after TRM officially acknowledged that a request for license plates would result in a premium credit without a reduction in coverage, it was National Union that continued to deny Textron's claim.

Any doubt about who was calling the shots was removed when one of the claim managers testified that the actual decision to deny the claim was made by one of

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[8] National Union was in no position to argue that it didn't know what TRM was doing. After all, the jury saw that National Union's own documents established that National Union's "senior" management "closely monitored" the bus insurance program. Likewise, National Union was in no position to argue that it didn't know coverage had been reinstated before the accident. After all, National Union's own documents established that National Union had electronic access to up-to-date policy information, and the original policy National Union maintained revealed that there never was any pre-accident deletion.

National Union's New York underwriters, not by TRM. In fact, the same underwriter who made the decision maintained National Union's Home Office policy – the policy National Union concealed from Textron and initially, even from National Union's own claims adjusters.

Far from ruling that TRM was the only one involved in the wrongdoing, the California Court of Appeal simply observed that because TRM was a managing agent for National Union, National Union was responsible for the conduct whether it was committed by TRM or National Union's own officials. As a result, the court expressly held that there was no need to even consider the evidence demonstrating National Union's own direct involvement in the wrongdoing. PA 25a.

The wrongdoing that led to this judgment was egregious. An insurance company found out about an accident. It verified coverage for the accident. But then it figured out that Ko barely spoke English and his broker did not know the difference between a lay-up credit (which maintains full coverage) and a "deletion" (which would have eliminated coverage). The insurance company then fabricated some documents and concealed many others in an effort to perpetrate a fraud. The insurance company used fraudulent documents to deny Ko's claim, Textron's claim, and the third-party liability claim that was presented by the insurer for the truck that the Textron-financed bus hit. The California Court of Appeal correctly noted that this kind of conduct can result in a five-year prison term *plus* a fine of up to double the amount involved in the wrongdoing. Cal. Pen. Code § 550. And on the civil or regulatory side, an insurance company that engages in such conduct can be subject to substantial fines or even a loss of its

ability to do business in the state. Cal. Ins. Code §§ 790.035 & 790.07.

Nevertheless, National Union argues in its petition that the California Court of Appeal looked only to the fact that insurance companies have long been subject to potential significant punitive damages in cases involving breach of the covenant of good faith and fair dealing. To the contrary, the California Court of Appeal expressly noted that fraudulent conduct by an insurance company is a felony that can result in imprisonment and serious fines. App. 30-31; cf. *Haslip*, 499 U.S. at 23 (noting that insurance fraud can result in imprisonment under Alabama law and approving a punitive damages award of more than 200 times out-of-pocket loss). In addition, California insurance companies have long known that a failure to act in good faith toward policyholders can result in significant punitive damages awards under California Civil Code § 3294. PA 31a. In making that observation, the California Court of Appeal followed *BMW v. Gore*.

As the California Court of Appeal properly observed, the $2,000 civil penalty that could have been assessed against BMW under the Alabama Deceptive Trade Practices Act would not have provided an out-of-state distributor with fair notice that its conduct might subject it to a multi-million dollar penalty because there was no "judicial decision in Alabama or elsewhere indicating that application of that policy might give rise to such severe punishment." *BMW*, 517 U.S. at 584; see App. 31. In contrast, California has long had several published judicial decisions that provide further warning to insurers as to the potential consequences of engaging in fraudulent or bad faith claims handling. PA 31a.

National Union has never argued it "lacked notice" that its conduct could result in a multi-million dollar punitive damages award. National Union could not seriously argue that it had no idea fabricating and concealing documents after an accident to try to make it look as if coverage had been removed before the accident could result in a multi-million punitive damages award. The third *BMW* guidepost was more than satisfied here.

CONCLUSION

Even if the jury's $10 million punitive damages verdict implicated constitutional questions, the judicially-reduced $1.7 million judgment did not. The post-accident doctoring of the insurance policy involved extremely reprehensible conduct. The ratio of punitive to compensatory damages was only 10:1. And when the harm and potential harm is considered, the ratio drops to 3:1 or less. The involved conduct would warrant serious criminal and civil penalties, including up to five years imprisonment and substantial fines on the criminal side, and substantial fines and potential loss of the insurer's license on the civil/regulatory side.

No one questions National Union's tenacity or willingness to fight. But this case has already been through two full rounds of appellate review. National Union is very fortunate that the trial court substantially reduced the jury's punitive damages verdict. But the trial court's significant reduction of punitive damages placed the ultimate judgment well within constitutional limits and

eliminated any conceivable reason for this Court's review. National Union's petition should be denied.

Respectfully submitted,

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IN THE SUPREME COURT OF CALIFORNIA

TEXTRON FINANCIAL CORPORATION, Plaintiff, Respondent, and Cross-Appellant vs. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, etc., et al. Defendant, Appellant, and Cross-Respondent.	**S095924** 4th Civ. No. G020323 OCSC No. 734096

* * *

ANSWER TO PETITION FOR REVIEW

* * *

Appeal from the Superior Court
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Honorable Raymond J. Ikola

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* * *

2. STATEMENT OF FACTS

National Union's Petition presents the "facts" in a selective and partial manner, ignoring evidence it deems unfavorable. National Union draws all inferences in its own favor, though it failed to convince the jury to draw those inferences at trial. As a result, Textron's discussion of facts is necessarily somewhat extended.

A. The Major Events

In early 1992, Textron loaned Il Sung Ko $87,000 to buy a tour bus for his business. To protect itself, Textron had Ko obtain insurance covering Textron's security interest in the bus. (R.T. 862-74; Ex. 2.) Ko bought insurance from National Union. Textron was an additional insured and a designated loss payee under the policy. (Ex. 198, pp. 45, 60-61.)

After the Los Angeles riots, Ko faced a slowing tourism business and cash flow problems. Douglas Ferguson, Ko's broker, advanced a premium payment for Ko. (R.T. 653, 660.) Nevertheless, on October 22, 1992, National Union sent Ko a notice of cancellation which said the policy would cancel as of November 27, 1992. (Ex. 10.) National Union did not give Textron notice of the cancellation.

Aware that Ko was not using some of the six buses in his fleet, Ferguson wrote to TRM International, Inc., National Union's managing general agent for bus insurance, and asked if a new policy could be issued "with only four units." (Ex. 14.) In response to Ferguson's inquiry, George Peare, a TRM underwriter, responded by suggesting a lay-up credit, a "much easier way of doing it." (Ex. 15.)

According to Ferguson, discussion about the lay-up credit was limited. Peare told him to "Get the license plates. Get the license plates." (R.T. 668.)

Lay-up credits are a form of mileage rating. The assumption is that the risk of loss is reduced where fewer total miles are being driven. An insurer that offers a lay-up credit reduces the premium when vehicles are not in regular use. (Ex. 236, pp. 50-56; R.T. 1550-51, 1783, 1789-90.) Unlike deletions, lay-up credits do not eliminate or reduce coverage.[1] When issuing lay-up credits, insurance companies typically ask for license plates to minimize the likelihood that a laid-up vehicle will be used on a daily basis. (Ex. 236, pp. 39-54; R.T. 1074, 1078-79, 1156-57, 1226, 3439.)

The lay-up credit was advantageous for National Union since it kept the policy in force, allowed National Union to continue collecting premium payments of about $5,000 a month, required very little paperwork, and did not require notice to other parties. In contrast, vehicle deletions would have required notice to Textron, other lenders, various public entities, and the City of Los Angeles. (Ex. 198, pp. 60-61, 95-96, 99.)

A few days after the policy cancelled for non-payment of premium (without notice to Textron), Ko made a partial

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[1] Deletions, on the other hand, eliminate coverage for the deleted vehicle. As a result, policyholders are not required to turn in license plates when the insurer deletes a vehicle from coverage. (R.T. 1690-91, 1697-98.) Deletions typically occur when a policyholder sells a vehicle to a third-party. (R.T. 832, 3932.) If insurance companies made policyholders turn in license plates when coverage was deleted, policyholders would not be able to sell their vehicles. (R.T. 1078-79, 1226, 3439.)

premium payment and sent the license plates for two of his six buses to Ferguson. Ferguson wrote to TRM on December 1, 1992, saying he had the plates for the "2 vehicles which are being deleted (suspended)." (Ex. 19.) The very next day, a lay-up credit was implemented and the policy was reinstated in full, with no reduction in coverage. (Ex. 20.)

Ko's broker, Ferguson, did not understand the difference between lay-up credits and suspensions, on the one hand, and deletions on the other. (R.T. 668-69.) Ferguson thought lay-up credits, suspensions, and deletions were all the same. (R.T. 690.) He incorrectly assumed that lay-up credits and suspensions terminated coverage.

Ferguson also wanted to make sure he recovered the premium he had advanced. So after National Union reinstated the policy, Ferguson continued to send notes to TRM which emphasized that he had the license plates. (Ex. 23.) However, since the lay-up credit had already been issued and the policy fully reinstated, TRM did not bother to respond.

On January 7, 1993, one of Ko's buses broke down. The Textron- financed bus was sent to pick up stranded passengers, and it was damaged in an accident. (R.T. 1347, Ex. 34.) Since Ferguson erroneously believed lay-up credits eliminated coverage, he told Ko (and his assistant, Mr. Adeyemo) the accident wasn't covered. (R.T. 695.) Nevertheless, after talking to a TRM claims supervisor, Dick Longuil, Ferguson presented a claim to National Union's adjusting affiliate, American International Adjustment Company (AIAC). (R.T. 695-97, 706-06.)

Because the lay-up credit had resulted in a full policy reinstatement, TRM verified coverage for the accident on

February 4, 1993. (Ex. 33.) But a Portland-based claims adjuster subsequently spoke to Ko's assistant and learned that Ko erroneously believed there was no coverage for the accident. The adjuster decided not to tell Ko's assistant that coverage had already been verified, explaining that "coverage is usually, in my experience, only discussed with an insured if it's a problem." (R.T. 1481.)

Claims adjusters had been instructed to contact John Lavin (an underwriting manager in National Union's Home Office) "for a complete policy copy." (Ex. 99.) The claims office did request a copy of the policy, but the request was refused. (R.T. 1464, 1506.)

Because National Union did not give adjusters access to the actual policy, claims personnel turned to a TRM claims supervisor, Dick Longuil.[2] But Longuil worked in New York, eight hours away from TRM's New Jersey office. (R.T. 697, 1647-48.) As a result, Longuil did not have access to the policy or any other file materials.

Even without documents, Longuil immediately had "a bad feeling about" the accident. (Ex. 26.) He was concerned about notice requirements (that obviously had not been

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[2] Throughout its Petition, National Union incorrectly argues that TRM had no involvement in claims. Actually, TRM had a staff claims supervisor, Dick Longuil. (R.T. 695.) TRM was deeply involved in one of the most important claim functions, verifications of coverage. (Ex. 33.) And National Union's claim representatives acknowledged that with respect to certain claim functions, TRM was "the only one that we have to rely on when it gets to this account." (R.T. 2832.) So it isn't surprising that TRM's president was a participant in the conference call that resulted in the final denial of Textron's claim. (R.T. 3108-12.)

satisfied), and the possibility of personal injury claims. (Ex. 30.)

Without giving adjusters a copy of the policy, National Union denied all claims pertaining to the accident on February 24, 1993. (Ex. 43.) The claims were denied even though coverage had been verified, and even though there were no documents or electronic information showing any "deletion." (Ex. 505; R.T. 2638-41.)

As of February 1993, no one had told Textron about the policy cancellation, the lay-up credit, the policy reinstatement, the accident, the coverage verification, or the denial of Ko's claim.

Ko continued making loan payments as long as he could. But by late 1993, Ko defaulted on his Textron loan. Textron then learned the bus might have been involved in an accident earlier that year. (R.T. 883-86, 996.) When it inquired, Textron was falsely told that the bus coverage was deleted before the accident. (R.T. 884.)

Textron presented its formal written claim by letter dated January 25, 1994. (Ex. 51.) Textron noted that it was not told about coverage termination until late in 1993. Textron's claim was denied, based on the false contention that National Union couldn't tell Textron about the coverage termination because National Union itself did not have advance notice of the cancellation. (R.T. 2325-27.) The denial letter did not disclose the lay-up credit, the reinstatement, or the fact that coverage had been verified after the accident. (Ex. 59.)

Textron started asking for a copy of the policy in January 1994. (Ex. 51.) Two months later, in March 1994, National Union finally gave its own claims adjusters a

microfiche copy of the original Home Office policy. (R.T. 606-07.) National Union decided to withhold it from Textron. (R.T. 2336, 2914, 3193, 3221.) Why did National Union refuse to let Textron see a copy of the original policy? Because the original policy had a credit endorsement, but no "deletion" endorsement. Rather than giving Textron a copy of the original policy, National Union gave Textron a different version of the policy. The new "certified" version of the policy replaced the credit endorsement No. 8 with a "deletion" endorsement No. 8.[3] (Ex. 78 p. 42, 198 p. 67; R.T. 968-70, 978-80, 2312-13.)

No witness who testified at trial could think of any legitimate reason for National Union to refuse Textron's request for the readily available original policy, while making Textron wait for a new and different version of the policy. (R.T. 3279, 3447-48.)

Meanwhile, in July 1994, National Union convened a conference call involving John Lavin (the underwriting manager charged with day-to-day supervision over TRM and responsibility for National Union's Division 20), Tom Spangenberg (TRM's president), and Ella Quinlan (a local

[3] The deletion endorsement was dated February 11, 1993. However, it was apparently created after October 5, 1993. The original policy was microfiched twice – once on March 3, 1993, and then again on October 5, 1993. (Ex. 198, p. 73, 88.) Since the original policy had no deletion endorsement, the inescapable inference was that the "deletion" endorsement was created at some point after October 5, 1993. This explained why the Portland claim file did not include a copy of the endorsement. (Ex. 505.) It also explained why Textron didn't receive a copy of the purported "deletion" endorsement until December of 1993. (Ex. 56; R.T. 946-47.) And it also explained why Ko (and his assistant, Adeyemo) did not receive any "deletion" version of endorsement No. 8. (R.T. 1356.)

claims manager). (Ex. 68, p. 2.) After concluding the lengthy conference call, Quinlan called Textron's counsel to say that Mr. Lavin was "adamant" that Textron's claim would never be voluntarily paid. (R.T. 2897-98, 3078.)

In August 1994, Spangenberg wrote to Don Schmitz, a National Union Home Office claims official. He described the incident as a "fiasco," and acknowledged the request for license plates. (Ex. 80.)

Textron sued National Union in August 1994. The jury found fraud by National Union. The findings included both affirmative misrepresentation and concealment. (C.T. 3714-21.) The jury also found National Union had acted in bad faith, and that it was guilty of malice, fraud *and* oppression. The jury awarded $10 million in punitive damages. (C.T. 4052-60.)

With these basic facts in mind, Textron briefly discusses several other parts of the record National Union has failed to discuss in its Petition.

B. National Union's Concealment Of Evidence And Deception

From start to finish National Union tried to conceal evidence and deceive Textron and others. When it started responding to Textron's claim, National Union chose not to mention important facts, such as the fact that the policy had been fully reinstated on December 2, 1992. (Exs. 20 & 59.) To prevent Textron from learning that the fabricated deletion endorsement had been created after the accident,

a "certificate of mailing" was placed over the purported creation date before the "deletion" version of endorsement No. 8 was sent to Textron. (Ex. 189; R.T. 614-15.)[4]

During the conference call where National Union's underwriters ordered denial of the claim, National Union decided to retain attorneys to try to shield documents from discovery. (Ex. 68, p. 2, R.T. 3622-23.) Then, instead of giving Textron a copy of the policy, National Union gave Textron a different version of the policy – a version which substituted a "deletion" endorsement for the lay-up credit endorsement.

During trial it also became clear that National Union's underwriting file had been manipulated before it was given to Textron.[5] The file manipulation was exposed because Ferguson's file included lay-up credit-related correspondence that had been removed from the underwriting file. For example, Exhibit 15 was George Peare's "much easier way of doing it" letter. The "much easier way of doing it" obviously referred to a lay-up credit. But

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[4] The "certificate of mailing" raised other serious questions. National Union incorrectly argued that this "certificate of mailing" showed that a "deletion" endorsement had been sent to Textron by certified mail, return receipt requested, in February 1993. (R.T. 2079.) But National Union never produced evidence of any return receipt, much less a return receipt signed by Textron. And curiously, there was no corresponding "certificate of mailing" for the other bus that was supposedly "deleted."

[5] Under the agreement between National Union and TRM, underwriting files were the property of National Union. (Ex. 170, ¶ 6(f).) Kay Marshall, an underwriter who worked for Lavin and Kelly in National Union's New York Home Office, verified production of the last part of the underwriting file to Textron on March 31, 1995. (R.T. 1669; C.T. 719.)

Exhibit 15 (and other documents) had been pulled from the underwriting file before the file was given to Textron. (R.T. 1623-24.)

National Union treated the Costa Mesa claim file (a file that included Textron claim materials) the same way. This claim file was Exhibit 231. It actually consisted of multiple volumes. But despite several court orders requiring production of the entire file, National Union refused to produce anything beyond the first volume of its claim file. Subsequent volumes of that claim file were never disclosed. (*E.g.*, Ex. 231; R.T. 201-09, 599, 2439-40, 2715, 3114-15; C.T. 619-21.)

During the trial National Union went so far as to destroy documents to keep them from the jury. For example, the initial 1993 Portland claim file included damaging information such as the post-accident coverage verification. National Union had improperly withheld the entire Portland claim file during discovery. But the court again ordered it produced during trial. (R.T. 204-209.)

The Portland file was originally housed in a jacket that would have reflected file transfer information, such as a transfer from the Portland claims office to National Union's Home Office in New York. (R.T. 1450-51, 2967.) Nevertheless, National Union produced only part of the file, explaining that "some idiot" had destroyed the file's jacket before it could be made available to Textron. (R.T. 2971, 3616, 4645.) There was no legitimate reason to destroy the jacket. And, in fact, without the jacket, there was nothing to hold the file together. (*Cf.*, Ex. 231.)

Attempts to deceive continued right up to the last day of trial, when National Union called a witness who tried to get the jury to believe Textron's claim had been paid (or

soon would be paid) in response to the jury's decision. (R.T. 4857-58.) Of course, to this very day, National Union has never paid any part of Textron's claim.

* * *

STATUTORY PROVISIONS INVOLVED

California Civil Code § 3294, subdivisions (a) & (c):

(a) In an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice, the plaintiff in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant.

* * *

(c) As used in this section, the following definitions shall apply:

(1) "Malice" means conduct which is intended by the defendant to cause injury to the plaintiff or despicable conduct which is carried on by the defendant with a willful and conscious disregard of the rights or safety of others.

(2) "Oppression" means despicable conduct that subjects a person to cruel or unjust hardship in conscious disregard of that person's rights.

(3) "Fraud" means an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.

California Civil Code § 3296:

(a) Whenever a judgment for punitive damages is entered against an insurer or health care service plan licensed pursuant to Chapter 2.2 (commencing with Section 1340) of Division 2 of the Health and Safety Code, the plaintiff in the action shall, within 10 days of entry of judgment, provide all of the following to the Commissioner of the Department of Insurance or the Director of the Department of Managed Health Care, whichever commissioner has regulatory jurisdiction over the insurer or health care service plan:

(1) A copy of the judgment.

(2) A brief recitation of the facts of the case.

(3) Copies of relevant pleadings, as determined by the plaintiff.

(b) The willful failure to comply with this section may, at the discretion of the trial court, result in the imposition of sanctions against the plaintiff or his or her attorney.

(c) This section shall apply to all judgments entered on or after January 1, 1995.

(d) "Insurer," for purposes of this section, means any person or entity transacting any of the classes of insurance described in Chapter 1 (commencing with Section 100) of Part 1 of Division 1 of the Insurance Code.

California Insurance Code § 769.85:

> The acts of the MGA are considered to be the acts of the insurer on whose behalf it is acting. An MGA may be examined as if it were the insurer.

California Insurance Code § 790.035:

> (a) Any person who engages in any unfair method of competition or any unfair or deceptive act or practice defined in Section 790.03 is liable to the state for a civil penalty to be fixed by the commissioner, not to exceed five thousand dollars ($5,000) for each act, or, if the act or practice was willful, a civil penalty not to exceed ten thousand dollars ($10,000) for each act. The commissioner shall have the discretion to establish what constitutes an act. However, when the issuance, amendment, or servicing of a policy or endorsement is inadvertent, all of those acts shall be a single act for the purpose of this section.
>
> (b) The penalty imposed by this section shall be imposed by and determined by the commissioner as provided by Section 790.05. The penalty imposed by this section is appealable by means of any remedy provided by Section 12940 or by Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code.

California Insurance Code § 790.07:

> Whenever the commissioner shall have reason to believe that any person has violated a cease and desist order issued pursuant to Section 790.05 or

a court order issued pursuant to Section 790.06, after the order has become final, and while the order is still in effect, the commissioner may, after a hearing at which it is determined that the violation was committed, order that person to forfeit and pay to the State of California a sum not to exceed five thousand dollars ($5,000) plus any penalty due under Section 790.05, which may be recovered in a civil action, except that, if the violation is found to be willful, the amount of the penalty may be a sum not to exceed fifty-five thousand dollars ($55,000) plus the penalty due under Section 790.05. For the purposes of this section, the failure to pay any penalty imposed pursuant to Section790.035 which has become final shall constitute a violation of the cease and desist order. For any subsequent violation of the cease and desist order or of the court order or the order to pay the penalty, while the order is still in effect, the commissioner may, after hearing, suspend or revoke the license or certificate of that person for a period not exceeding one year; provided, however, no proceeding shall be based upon the subsequent violation unless the same was committed or continued after the date on which the order imposing the penalty pursuant to the preceding paragraph became final. The hearings provided by this section shall be conducted in accordance with the Administrative Procedure Act, except that the hearings may be conducted by an administrative law judge in the administrative law bureau when the proceedings involve a common question of law or fact with another proceeding arising under other Insurance Code sections that may be conducted by administrative law bureau administrative law judges. The commissioner and the appointed administrative law judge shall have all the powers

granted under the Administrative Procedure Act. The person shall be entitled to have the proceedings and the order of the commissioner therein reviewed by means of any remedy provided by Section 12940 or by the Administrative Procedure Act.

California Penal Code § 550, subdivisions (b) & (c) (pertinent parts):

(b) It is unlawful to do, or to knowingly assist or conspire with any person to do, any of the following:

(1) Present or cause to be presented any written or oral statement as part of, or in support of or opposition to, a claim for payment or other benefit pursuant to an insurance policy, knowing that the statement contains any false or misleading information concerning any material fact.

(2) Prepare or make any written or oral statement that is intended to be presented to any insurer or any insurance claimant in connection with, or in support of or opposition to, any claim or payment or other benefit pursuant to an insurance policy, knowing that the statement contains any false or misleading information concerning any material fact.

(3) Conceal, or knowingly fail to disclose the occurrence of, an event that affects any person's initial or continued

right or entitlement to any insurance benefit or payment, or the amount of any benefit or payment to which the person is entitled.

* * *

(c)(3) Every person who violates paragraph (1), (2), (3), or (4) of subdivision (b) shall be punished by imprisonment in the state prison for two, three, or five years, or by a fine not exceeding fifty thousand dollars ($50,000), unless the value of the fraud exceeds fifty thousand dollars ($50,000), in which event the fine may not exceed double the value of the fraud, or by both that imprisonment and fine; or by imprisonment in a county jail not to exceed one year, or by a fine of not more than one thousand five hundred dollars ($1,500), or by both that imprisonment and fine.

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No. 02-966

In The
Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

vs.

TEXTRON FINANCIAL CORPORATION,

Respondent.

On Petition For A Writ Of Certiorari To The Court Of Appeal Of California, Fourth Appellate District

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REPLY BRIEF FOR PETITIONER

National Union's petition presents the issues whether, as applied by the lower courts, the second and third *BMW* guideposts provide fair notice of the severity of the penalty likely to be imposed for prohibited conduct and meaningful guidance for appellate review of punitive damage awards. *See BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 574-575 (1996). As we demonstrated, although this court has indicated that punitive damages may exceed a low multiple of compensatory damages only in certain limited circumstances, *id.* at 582, the lower courts, like the Court of Appeal in this case, frequently uphold punitive damage awards that substantially exceed compensatory damages without regard to whether those circumstances are present. In addition, we demonstrated that although this court directed courts to look to legislatively imposed sanctions for comparable misconduct in determining whether a punitive damage award is excessive, *id.* at 583, many lower courts, like the Court of Appeal here, hold that a defendant received fair notice its conduct could subject it to a significant punitive damage award so long as similar awards had been imposed in prior cases. We explained that this analysis is circular and illogical because it ignores the fact that excessive punitive damage awards were precisely the problem that prompted this court to impose constitutional limitations on the size of punitive damage awards.

Textron's brief in opposition (Opp.) barely touches on these issues. Rather, in a fact-intensive response, it appears to argue that National Union's conduct was so egregious that the legal discussion in the petition is beside the point. However, Textron, like National Union, must

deal with the issues framed by the opinion of the Court of Appeal.

1. Textron made the same accusations of egregious conduct against National Union in the Court of Appeal and they were strenuously disputed by National Union. However, the Court of Appeal never decided whether the accusations were supported by substantial evidence. Rather, it held the $1.7 million punitive damage award was proper because there was substantial evidence that TRM International, an independent company that acted as National Union's underwriter, engaged in that conduct, and National Union was vicariously liable. App. 22-25. "In light of this conclusion it is unnecessary to consider National Union's additional claims concerning . . . alleged insufficiency of the evidence based on its own conduct." App. 25; *see also* App. 29 ("Simply describing National Union's liability as vicarious does not militate against imposing a proportionately appropriate punitive damage award against it based on TRM's wrongdoing.").

If, as Textron appears to implicitly concede, the $1.7 million punitive damage award passes constitutional muster only if National Union itself engaged in the conduct described in Textron's brief in opposition, the judgment of the Court of Appeal should be vacated and the case remanded to that court so that it can decide whether Textron's accusations are supported by substantial evidence.

2. Textron fails to respond to our argument that, as presently applied by the lower courts, the second *BMW* guidepost, the "ratio to the actual harm inflicted on the plaintiff," *see BMW*, 517 U.S. at 580, does not provide meaningful guidance for appellate review of punitive

damages. Although, as Textron notes, Opp. 14, some courts have refused to limit punitive damages to a single digit multiplier of compensatory damages, *e.g.*, *Cooper v. Casey*, 97 F.3d 914, 919 (7th Cir. 1996), other courts have struck down as constitutionally excessive punitive damage awards that greatly exceed the 4 to 1 ratio this court in *Pac. Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1, 23-24 (1991) held was "close to the line . . . of constitutional impropriety." *See, e.g.*, *In re Exxon Valdez*, 270 F.3d 1215, 1243-44 (9th Cir. 2001). Textron may disagree with National Union as to the correct answer, but it cannot reasonably dispute that in light of the divergent opinions in the lower courts, clarification from this court is required if the second *BMW* guidepost is to provide fair notice of the severity of the penalty likely to be imposed for prohibited conduct and meaningful guidance for appellate review of punitive damages.

3. Textron accuses National Union of inaccurately calculating the ratio between compensatory and punitive damages. Opp. 15. However, it does not challenge National Union's assertion that the ratio must be determined by looking only to the count on which punitive damages were awarded, *see Zimmerman v. Direct Fed. Credit Union*, 262 F.3d 70, 82 n.9 (1st Cir. 2001); that under California law, a punitive damage award may be based only on an award of tort damages, not contract damages, *see Myers Bldg. Indus. Ltd. v. Interface Tech.*, 17 Cal. Rptr. 2d 242, 248 (Ct. App. 1993); or that the total *tort* damages awarded in this case were $89,000 – the $61,500 in policy benefits plus interest were awarded on Textron's breach of contract cause of action, not its tort cause of action for bad faith. App. 6. Consequently, looking only to the cause of action

on which punitive damages were awarded, the ratio was 20 to 1.

4. Textron argues that the potential harm that could have resulted from the conduct in this case substantially exceeded the $89,000 in tort damages awarded by the jury. According to Textron, although its bad faith damages included only $86,000 in attorneys' fees and costs, those fees would have been substantially higher if it had paid its attorneys by the hour, rather than pursuant to a contingency agreement. Asserting that its attorneys spent over 1,500 hours to recover policy benefits, Textron says that if it had paid them on an hourly basis, its recoverable attorneys' fees, *i.e.*, its tort damages, would have exceeded $500,000. Opp. 17.

This contention is without merit. Under California law, the only attorneys' fees recoverable as tort damages in an insurance bad faith action are those fees necessarily incurred to recover policy benefits. "Fees attributable to obtaining any portion of the plaintiff's award which exceeds the amount due under the policy are not recoverable." *Brandt v. Superior Court*, 693 P.2d 796, 800, 210 Cal. Rptr. 2d 211, 215 (1985). The determination whether Textron was entitled to policy benefits presented a pure question of law – whether the policy permitted National Union to terminate Textron's rights as a loss payee without advance notice to Textron – which the trial court decided on the basis of legal briefs and oral argument. App. 6. The 1,500-plus hours of attorney time allegedly devoted to the case by Textron's attorneys were not incurred to obtain a favorable ruling on that narrow legal issue, but in order to recover punitive damages by establishing a complicated "post-accident underwriting" scheme between TRM and Ferguson, the insured's broker.

Consequently, even if Textron's attorneys had charged by the hour, Textron's damages could not have included $500,000 in attorneys' fees because those fees would not have been attributable to obtaining policy benefits.

5. Textron also argues that the potential harm from the conduct in this case exceeded $89,000 because (a) the denial of coverage caused Ko to declare bankruptcy, Opp. 17, and (b) if the bus accident had caused personal injuries, and if the TRM/Ferguson post-accident underwriting scheme had succeeded, there would have been no insurance coverage for those injuries. Opp. 17-18. The contention is without merit for several reasons.

First, there was no evidence that the denial of the claim for the damage to the bus caused Ko's bankruptcy.

Second, even if the post-accident underwriting scheme had succeeded, the National Union policy still would have provided coverage for any personal injuries suffered in the accident. Under California law, liability coverage for a commercial vehicle remains in effect until 30 days after the Public Utilities Commission receives a written notice that a policy has been canceled. Without that notice, a deletion endorsement, no matter when it is prepared, has absolutely no effect on liability coverage. Cal. Pub. Util. Code § 4667 (West 1994); *see also* Cal.Veh. Code § 34630(b) (West 2000); *Transamerica Ins. Co. v. Tab Transp., Inc.*, 906 P.2d 1341, 48 Cal. Rptr. 2d 159 (1995).

Third, and most significantly, while this court has held that a court may consider the potential as well as the actual harm from the defendant's conduct in determining whether a punitive damage award is excessive, it has nonetheless emphasized that the focus must be on the potential harm *to the plaintiff*, not to other persons who

are not parties to the lawsuit. *See, e.g., TXO Prod. Corp. v. Alliance Res. Corp.*, 509 U.S. 443, 460 (1993) (courts may "consider the magnitude of the *potential harm* that the defendant's conduct would have caused to *its intended victim* if the wrongful plan had succeeded") (first emphasis in original, second added); *BMW*, 517 U.S. at 581 (summarizing *TXO* as having "relied on . . . the harm *to the victim* that would have ensued if the tortious plan had succeeded") (emphasis added); *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 435 (2001) (the relevant determination for ratio purposes is "the relationship between the penalty and the harm to the victim caused by the defendant's actions"); *see also id.* at 440 (courts must consider, among other things, "the disparity between the harm (or potential harm) suffered by the plaintiff and the punitive damages award").

While misguided, Textron's attempt to justify the ratio in this case by reference to the potential harm allegedly faced by third persons is instructive. It shows that, notwithstanding this court's prior decisions, there is still considerable confusion regarding proper application of the second *BMW* guidepost. Thus, Textron's answer demonstrates that certiorari should be granted to clarify that in applying that guidepost, a court should focus on the actual and potential harm *to the plaintiff* from the defendant's conduct, not the harm that the defendant's conduct potentially could have caused to persons who were not parties to the lawsuit.

6. Textron fails to meaningfully respond to our showing that, as applied by the lower courts, the third *BMW* guidepost, the comparison between "the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct . . .," *BMW*,

517 U.S. at 583, similarly fails to afford the fair notice required by due process and is essentially meaningless as a check on grossly excessive punitive damages. It simply repeats the Court of Appeal's conclusion that the punitive damage award here was not constitutionally excessive when examined under that guidepost because similar awards had been imposed on insurers in prior cases. Opp. 24. Textron fails to address our argument that this analysis is circular and illogical because excessive punitive damage awards were precisely the problem this court was seeking to rectify in *BMW*, 517 U.S. 559, when it adopted three guideposts for determining whether a punitive damage award is constitutionally excessive.

Textron also refers to the statutory penalties that could be imposed for the alleged conduct in this case. Opp. 24. However, those penalties could have been imposed on National Union only if it personally engaged in the prohibited conduct. As we have shown, the Court of Appeal did not decide whether the accusation that National Union engaged in that conduct was supported by substantial evidence. Instead, it held that the punitive damage award was constitutional because National Union was vicariously liable for TRM's conduct. App. 22-25, 29. Thus, the statutory penalties cited by Textron cannot support the $1.7 million punitive damage award.

CONCLUSION

For the foregoing reasons, and for those in the petition, the petition for writ of certiorari should be granted. In the alternative, the petition should be granted, the judgment of the Court of Appeal vacated, and the case

remanded for further consideration in light of this court's decision in *State Farm Mutual Automobile Ins. Co. v. Campbell*, No. 01-1289.

Respectfully submitted,

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